

LOSING OUR RELIGION: REEVALUATING THE SECTION 501(c)(3) EXEMPTION OF RELIGIOUS ORGANIZATIONS THAT DISCRIMINATE

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INTRODUCTION

In the last several decades, religious organizations have come to occupy an enviable legal stature in American society, leading one legal scholar to comment that “separation of church and state is no longer the law of the land.”¹ According to one analysis, religious organizations received over two hundred exemptions and other regulatory benefits in federal legislation over the last eighteen years, covering a wide array of areas such as pensions, immigration, and land use.² One special break enacted to prevent religious discrimination in local zoning not only eliminated the discrimination, but also provided churches with the ability to discriminate against other landowners.³ Beginning with a policy shift in 1996 under President Bill Clinton and continuing under President George W. Bush’s Faith Based Initiative, religious organizations’ receipt of state and federal government grants and contracts has steadily increased.⁴ In addition to these more recently bestowed benefits, religious organizations, including churches, enjoy a longstanding exemption from federal income tax as “charitable organizations”⁵ and are a primary beneficiary of the charitable contributions

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¹ Diana B. Henriques, *As Exemptions Grow, Religion Outweighs Regulation*, N.Y. TIMES, Oct. 8, 2006, at A1 [hereinafter Henriques, *Exemptions Grow*] (quoting John Witte, Jr., Director of the Center for the Study of Law and Religion at the Emory University Law School).

² *Id.*

³ *Id.* The Religious Land Use and Institutionalized Persons Act of 2000 provided churches with a greater ability to challenge local zoning decisions in court. Pub. L. No. 106-274, 114 Stat. 803 (codified in scattered sections of 42 U.S.C.). Professor Marci A. Hamilton, who calls for increased consideration of religious exemptions, commented that the Act gave “such an expansive remedy that not only are [churches] not getting discriminated against, but they are now capable of discriminating against all other landowners.” Henriques, *Exemptions Grow*, *supra* note 1.

⁴ Henriques, *Exemptions Grow*, *supra* note 1.

⁵ See Nicholas A. Mirkay, *Is It “Charitable” to Discriminate? The Necessary Transformation of Section 501(c)(3) into the Gold Standard for Charities*, 2007 WIS. L. REV. 45,

deduction.⁶ In 2006, that deduction alone cost the federal government \$40 billion in lost revenue and outweighed government expenditures on public lands' preservation, environmental protection, and new energy development.⁷

In addition to the above benefits, additional exemptions and benefits have been proposed in pending congressional legislation. One such bill, the Houses of Worship Free Speech Restoration Act of 2005, would amend the Internal Revenue Code (Code) to exempt churches and "other houses of worship"⁸ from the political campaign activity prohibition in § 501(c)(3).⁹ The Workplace Religious Freedom Act of 2005 would amend the Civil Rights Act of 1964¹⁰ to require employers "to initiat[e] and engage" in an affirmative and bona fide effort, to reasonably accommodate" the religious practices of employees.¹¹ Another congressional bill would amend the Higher Education Act to prevent educational accreditation boards from requiring private religious schools to comply with applicable state and local nondiscrimination laws.¹² Most recently, religious organizations would be exempt from the prohibition on sexual

56–60 [hereinafter Mirkay, *Charities & Discrimination*], for a discussion of the meaning of "charitable" under § 501(c)(3) of the Internal Revenue Code and the common practice of collectively referring to the entities listed in the statute (e.g., religious, educational, scientific, etc.) as "charitable." This Article uses the terms "charitable organization," "religious organization," and "tax-exempt organization" to refer to nonprofit organizations that qualify for, and have been granted, an exemption from federal income tax. *See generally* I.R.C. § 501(c)(3) (2000) (explaining eligibility for these tax benefits). In addition, the terms "exemption" and "tax-exempt status" refer exclusively to federal income tax law and do not imply exemption under other federal tax laws, or under state or local laws, unless otherwise indicated.

⁶ I.R.C. § 170(c)(2) (2000); *see* Ellen P. Aprill, *Churches, Politics, and the Charitable Contribution Deduction*, 42 B.C. L. REV. 843, 845 (2001) (reporting that religious organizations received sixty percent of all charitable contributions made in 1998, which represented the "largest share of any category of charitable organizations, as well as the largest average contribution, \$1,002" (citation omitted)).

⁷ Stephanie Strom, *Big Gifts, Tax Breaks and a Debate on Charity*, N.Y. TIMES, Sept. 6, 2007, at A1.

⁸ Houses of Worship Free Speech Restoration Act of 2005, H.R. 235, 109th Cong. (2005); *see* Diana B. Henriques, *In the Congressional Hopper: A Long Wish List of Special Benefits and Exemptions*, N.Y. TIMES, Oct. 11, 2006, at A20 [hereinafter Henriques, *Long Wish List*]; *see also* Religious Freedom Act of 2006, S. 3957, 109th Cong. (2006); Diane Freda, *Inhofe Measure Introduced to Allow Clergy to Speak Out on Political Issues*, 189 DAILY TAX REP. (BNA) G-7 (Sept. 29, 2006).

⁹ Unless otherwise indicated, all "Section" references herein are to the Internal Revenue Code of 1986, as amended.

¹⁰ 42 U.S.C. § 2000e(j) (2000).

¹¹ Workplace Religious Freedom Act of 2005, H.R. 1445, 109th Cong. (2005); *see also* Henriques, *Long Wish List*, *supra* note 8.

¹² *See* Paul Johnson, *Congress Moves to Except Religious Schools from Gay Rights Laws*, 365 GAY.COM, Apr. 18, 2006, available at Posting of Bill Howe to NAMEblog, http://nameorg.org/pipermail/name-mce_nameorg.org/2006-April/000889.html (Apr. 26, 2006, 11:02 EDT).

orientation discrimination in the workplace under the Employment Non-Discrimination Act of 2007.¹³

On the state and local levels, religious organizations also typically enjoy lucrative real property tax exemptions.¹⁴ For example, in Colorado, religiously owned real property valued at more than \$1 billion was exempt from local property taxes in 2006.¹⁵ These exemptions are being extended as religious organizations expand their mission to encompass multimedia operations, biblical theme parks, retirement communities, child care facilities, fitness centers, bookstores, and coffee shops.¹⁶ Considering these expanded missions, the propriety of religious organizations' tax exemption is being questioned¹⁷ given that these organizations still depend on, and consume, the same public services as taxpaying citizens, effectively shifting the cost of providing those public services onto those citizens.¹⁸

The propriety of the extensive tax and other legal exemptions enjoyed by religious organizations must further be questioned when they maintain discriminatory policies or engage in discriminatory practices.¹⁹ Discrimination can be legally defined as "a failure to treat all persons equally when no reasonable distinction can be found between those favored and those not favored."²⁰ Based on that definition, religious organizations discriminate not only in the employment context, which is legally sanctioned in certain circumstances,²¹ but also in services or activities considered part of their religious mission, such as education.²² Many of the discriminatory acts and policies involve affiliated schools and universities that (i) terminated employees for questioning or violating church doctrine on sexual orientation or marital status, (ii) expelled

¹³ Employment Non-Discrimination Act of 2007, H.R. 3685, 110th Cong. (2007); *see also* H.R. 2015, 110th Cong. § 6 (2007) (including gender identity as a protected class); *Vote On ENDA Delayed as LGBT Pressure Mounts*, 365Gay.com, Oct. 1, 2007, available at Posting of 365GAY.COM Newscenter Staff to Ray's List, http://rayslistgbltnews.blogspot.com/2007_09_30_archive.html (Oct. 1, 2007, 19:00 EST) (stating support for legislation banning discrimination).

¹⁴ *See generally* Diana B. Henriques, *As Religious Programs Expand, Disputes Rise Over Tax Breaks*, N.Y. TIMES, Oct. 10, 2006, at A1 [hereinafter Henriques, *Religious Programs*] (describing various real property tax breaks for church-held property).

¹⁵ *Id.* The total forgone property tax revenue on religiously owned real property is not available, nor is how much of that forgone revenue is shifted to other taxpaying landowners. *Id.*

¹⁶ *Id.* Whether these expanded activities are exempt from applicable property taxes typically depends on the state's definition or concept of "charity." *Id.*

¹⁷ *See id.* (describing discontentment in communities about some charitable tax deductions).

¹⁸ Henriques, *Exemptions Grow*, *supra* note 1. The total national cost of providing such public services is not readily known. *Id.*

¹⁹ *See infra* text accompanying notes 24–40 (discussing various discriminatory practices of religious organizations).

²⁰ BLACK'S LAW DICTIONARY 500 (8th ed. 2004).

²¹ *See infra* notes 194–95 and accompanying text.

²² *See Henriques, Religious Programs*, *supra* note 14.

students for their alleged or announced gay sexual orientation, or (iii) maintained employment and admissions standards that discriminated on the basis of sexual orientation or marital status.²³ Consider some additional recent examples:

1. Massachusetts Roman Catholic bishops requested that Catholic Charities and Catholic social service agencies be granted an exemption from the state's anti-discrimination law that permits gay and lesbian individuals to adopt children.²⁴ The four Roman Catholic bishops in the state asserted that the law violated their constitutionally granted religious freedom.²⁵ Eight members of the Catholic Charities board eventually resigned in protest of the bishops' position.²⁶ The Roman Catholic Archdiocese of San Francisco has similarly made statements that its Catholic Charities agency "will no longer allow same-sex couples to adopt children," threatening its receipt of \$5.8 million in state and local government funding.²⁷

2. A Jewish university withdrew financial support for the student club, Gay-Straight Alliance, and barred the organization from using the university's name.²⁸ A university officer stated that gay lifestyle did not comport with "observant Judaism" and the university's values.²⁹ Similarly, a Roman Catholic-affiliated medical college opposed recognition of a gay and lesbian club because it would "'advocate and promote activities inconsistent with the values of the college.'"³⁰

3. A physician filed suit against his employer, a Roman Catholic-affiliated hospital, for its refusal to grant his life partner coverage under its employee health insurance policy.³¹ The physician and the hospital maintain conflicting viewpoints on the applicability of Connecticut's civil union statute to the dispute.³² The hospital defends its decision as complying with the Roman Catholic Church's "'teachings, principals [sic] and ethical directives.'"³³

²³ See Mirkay, *Charities & Discrimination*, *supra* note 5, at 48–50.

²⁴ See *Uproar In Boston Over Gay Adoptions*, CBS NEWS, Mar. 2, 2006, http://www.cbsnews.com/stories/2006/03/02/national/main1361889.shtml?source=search_story; see also Jonathan Saltzman, *Romney Eyes Bill Exempting Religious Groups on Bias Laws*, BOSTON GLOBE, Mar. 11, 2006, at A4.

²⁵ *Boston Archdiocese Stops Adoption Work*, CBS NEWS, Mar. 11, 2006, http://www.cbsnews.com/stories/2006/03/11/national/main1391621.shtml?source=search_story.

²⁶ *Id.*

²⁷ Wyatt Buchanan, *Archdiocese Halts Same-Sex Adoptions at Catholic Charities; Spokesman Points to Stance Taken by New Archbishop*, S.F. CHRON., Mar. 21, 2006, at B2.

²⁸ See Chris G. Denina, *Gay Club Loses Touro OK*, VALLEJO TIMES HERALD (Cal.), Sept. 29, 2006, at A1.

²⁹ *Id.*

³⁰ Andy Newman, *Westchester Not Examining Barring of Gay Student Club*, N.Y. TIMES, Mar. 31, 2005, at B4 (quoting statement from New York Medical College).

³¹ Michael Puffer, *Gay Complaint May Pit State Against Church*, WATERBURY REPUBLICAN-AM. (Conn.), Feb. 5, 2006, available at <http://www.freerepublic.com/focus/f-news/1572459/posts>.

³² See *id.* (stating that the couple believed the hospital was compelled to cover the couple because Connecticut recognized civil unions).

³³ *Id.* (quoting Robert Ritz, President and CEO of Saint Mary's Hospital).

4. An evangelical Christian-owned university that encouraged a part-time professor to apply for a full-time position allegedly rejected her for being openly gay.³⁴ The university's president explained that the university only hired Christians who observed the church's principles, one of which stated that only heterosexuals should marry and have sexual relations.³⁵

5. A Roman Catholic all-girls secondary school compelled two lesbian employees to resign or be fired after they distributed invitations to their commitment ceremony.³⁶

6. A full professor resigned from a non-denominational evangelical Protestant college rather than conform to the college's longstanding policy on divorced employees.³⁷ Under that policy, the professor would have been required to discuss the terms of his divorce with the college to determine whether his marital dissolution fell within what the college deemed to be acceptable biblical parameters.³⁸

7. A Roman Catholic-affiliated university rejected adding sexual orientation to its stated nondiscrimination policy that applied to the hiring and promotion of faculty and staff as well as student admissions.³⁹ A statement issued by the university's trustees explained that the inclusion of sexual orientation in its policy could restrain its ability to "make decisions that are necessary to support Catholic church teaching."⁴⁰

The paramount issue raised by these examples of discrimination is continued federal governmental support⁴¹ of the religious organizations via tax-exempt status

³⁴ See Angela Rozas, *North Park Sued; Sex Bias Charged; Gay Professor Accuses College*, CHI. TRIB., Dec. 4, 2003, at C2.

³⁵ *Id.*; *North Park Accused of Discrimination*, CHI. TRIB., Dec. 4, 2003, at 6.

³⁶ Manuela Da Costa-Fernandes, *Lesbians' Firing Fuels Outrage*, NEW HAVEN REG., July 2, 2002, available at <http://www.nhregister.com/articles/2002/07/02/import/4619710.txt>.

³⁷ Elizabeth Redden, *Divorce: Grounds for Dismissal*, INSIDE HIGHER ED., Apr. 25, 2008.

³⁸ *Id.*

³⁹ Chuck Colbert, *Notre Dame Blew It on Discrimination Policy*, NAT'L CATHOLIC REP., Mar. 26, 1999, available at http://natcath.org/NCR_Online/archives2/1999a/032699/032699k.htm. In contrast, the anti-discrimination policy of Saint Louis University, a Catholic Jesuit university specifically states: "Based on our Catholic values and tradition we are committed to protecting the dignity of each person and therefore extend our nondiscrimination policy to include sexual orientation." Saint Louis University Antidiscrimination Policy, available at http://www.slu.edu/organizations/rainbow/slu_policy.html. Similarly, Boston College, also a Catholic Jesuit university, provides that it is the policy of the college

to comply with all state and federal laws prohibiting discrimination in employment and in its educational programs on the basis of a person's race, religion, color, national origin, age [sic] sex, marital or parental status, veteran status, or disability, and to comply with state law prohibiting discrimination on the basis of a person's sexual orientation.

Notice of Nondiscrimination, Boston College Office for Institutional Diversity, available at <http://www.bc.edu/offices/diversity/compliance/nondiscrim.html> (last visited Nov. 23, 2008).

⁴⁰ Colbert, *supra* note 39 (quoting statement of Notre Dame trustees).

⁴¹ For further discussion on the equivalence of tax exemption and the charitable contributions deduction to "subsidies" or direct government grants of money, see Mirkay, *Charities & Discrimination*, *supra* note 5, at 79–82; see also David A. Brennen, *Tax*

and a charitable contributions deduction for their donors.⁴² Current federal income tax law does not explicitly prohibit discrimination by religious organizations.⁴³ “The only possible restraint on discrimination exists in the public-policy doctrine enunciated by the U.S. Supreme Court in *Bob Jones University v. United States*, which granted the Treasury Department (and the IRS by delegation) the power to revoke the tax-exempt status of an organization whose purpose violates ‘established public policy.’”⁴⁴ However, the IRS has used the doctrine to revoke tax-exempt status only in instances where the “organizations . . . participated in racial discrimination, advocated civil disobedience, or involved themselves in an illegal activity.”⁴⁵ Despite its merits, the doctrine’s main failure is its lack of a clearly defined source of “established public policy.”⁴⁶ For instance, based on examples of discrimination provided herein, does discrimination on the basis of sexual orientation or marital status violate an established public policy?⁴⁷ Legal scholars differ in their conclusions.⁴⁸ Furthermore,

Expenditures, Social Justice, and Civil Rights: Expanding the Scope of Civil Rights Laws to Apply to Tax-Exempt Charities, 2001 BYUL REV. 167, 173, 208–25 [hereinafter Brennen, *Tax Expenditures*] (discussing both the legal effects of economic equivalence and the constitutional equivalence tax expenditure theories).

⁴² Religious organizations are typically exempt from federal income taxation pursuant to § 501(c)(3). I.R.C. § 501(c)(3) (2000). As eligible organizations described in § 170(c)(2), religious organizations may receive tax-deductible charitable contributions pursuant to § 170(a). I.R.C. § 170(a), (c)(2)(B) (2000).

⁴³ See Mirkay, *Charities & Discrimination*, *supra* note 5, at 51; see also Brennen, *Tax Expenditures*, *supra* note 41, at 169.

⁴⁴ Mirkay, *Charities & Discrimination*, *supra* note 5, at 51 (quoting *Bob Jones Univ. v. United States*, 461 U.S. 574, 586 (1983)).

⁴⁵ *Id.*; see also David A. Brennen, *The Power of the Treasury: Racial Discrimination, Public Policy, and “Charity” in Contemporary Society*, 33 U.C. DAVIS L. REV. 389, 391 n.2 (2000) [hereinafter Brennen, *Racial Discrimination*] (citing Rev. Rul. 75-384, 1975-2 C.B. 204; Rev. Rul. 71-447, 1971-2 C.B. 230; I.R.S. Gen. Couns. Mem. 39,862 (Dec. 2, 1991)).

⁴⁶ Mirkay, *Charities & Discrimination*, *supra* note 5, at 51, 67; see also Brennen, *Racial Discrimination*, *supra* note 45, at 403–04, 407, 439 (describing the problems surrounding defining “established public policy”).

⁴⁷ See Mirkay, *Charities and Discrimination*, *supra* note 5, at 51 (asking if this policy extends to include sexual orientation or marital status).

⁴⁸ *Id.*; see also Gay Rights Coal. of Georgetown Univ. Law Ctr. v. Georgetown Univ., 536 A.2d 1, 38–39 (D.C. Ct. App. 1987) (holding that Georgetown University violated a District of Columbia law prohibiting an educational institution from discriminating against an individual on the basis of sexual orientation, and concluding that the “eradication of sexual orientation discrimination is a compelling governmental interest”); BRUCE R. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* § 6.2(d) (9th ed. 2007) (“It may also be quite validly asserted that there is a federal public policy, either presently in existence or in the process of development, against other forms of discrimination, such as discrimination on the basis of marital status, national origin, religion, handicap, sexual preference, and age.” (citation omitted)). But cf. Michael Hatfield et al., *Bob Jones University: Defining Violations of Fundamental Public Policy*, in 6 TOPICS IN PHILANTHROPY 1, 86–87 (2000), available at <http://www1.law>

critics routinely comment that the public policy doctrine places too much discretion in a regulatory agency.⁴⁹

In a prior article, I proposed a solution to the problem of discrimination by charitable organizations (a term commonly interpreted to include religious organizations)⁵⁰—enact a broad and well-defined nondiscrimination requirement in § 501(c)(3).⁵¹ This nondiscrimination provision would be based on currently existing language in the federal civil rights laws, but “expanded to include the bases on which charitable organizations most commonly discriminate”: sexual orientation and marital status.⁵² “Inherent in this proposal is the notion that any discrimination by a charitable organization is intrinsically incompatible with that organization’s charitable purpose and mission.”⁵³ The inclusion of a nondiscrimination requirement directly in the statute that grants tax-exempt status sends a strong and symbolic message to potential and existing charitable organizations that discriminatory policies and practices are intrinsically inconsistent

.nyu.edu/ncpl/library/publications/Monograph2000BobJones.pdf (concluding that there is no “fundamental national public policy against sexual orientation discrimination”).

⁴⁹ See Brennen, *Tax Expenditures*, *supra* note 41, at 186–87; Brennen, *Racial Discrimination*, *supra* note 45, at 411–28, 446; Charles O. Galvin & Neal Devins, *A Tax Policy Analysis of Bob Jones University v. United States*, 36 VAND. L. REV. 1353, 1372–73 (1983).

⁵⁰ See Mirkay, *Charities & Discrimination*, *supra* note 5. The Supreme Court’s decision in *Bob Jones University v. United States*, 461 U.S. 574 (1983), solidified the view that a common law “charitable” overlay to all exempt organizations described in § 501(c)(3) existed. *Id.* at 585–86. It noted that in order to qualify for exempt status thereunder, an organization must (1) fall within one of the eight categories set forth in the statute, and (2) demonstrate that its activities are not contrary to established public policy. *Id.* at 585. In rejecting the university’s argument that the eight categories in § 501(c)(3) are disjunctive and, therefore, that an organization need not also qualify as “charitable” to be tax-exempt, the Court explained that Congress intended that “entitlement to tax exemption depends on meeting certain common-law standards of charity—namely, that an institution . . . must serve a public purpose and not be contrary to established public policy.” *Id.* at 586; see also John Witte, Jr., *Tax Exemption of Church Property: Historical Anomaly or Valid Constitutional Practice?*, 64 S. CAL. L. REV. 363, 376 n.49 (1991) (discussing the historical evolution and eventual inclusion of “religious use” of property into “charitable use”); cf. Miriam Galston, *Public Policy Constraints On Charitable Organizations*, 3 VA. TAX REV. 291, 292 (1984) (arguing the debate should be narrowed to consider policy considerations of §§ 501(c)(3) and 170, not the policy as a whole).

⁵¹ Mirkay, *Charities & Discrimination*, *supra* note 5, at 52, 84. For recent examples of discrimination by charitable and religious organizations, see *supra* notes 24–43 and accompanying text, and Mirkay, *Charities & Discrimination*, *supra* note 5, at 48–50.

⁵² Mirkay, *Charities & Discrimination*, *supra* note 5, at 84. Any statutorily imposed nondiscrimination requirement should address the intended meaning of “discrimination” with respect to discriminatory organizations that otherwise operate exclusively for exempt purposes under § 501(c)(3). *Id.* at 103–04 (“Ultimately, whether or not a particular policy or action constitutes discrimination would depend on a facts-and-circumstances determination, with standards and burdens of proof borrowed from established civil-rights laws and other nondiscrimination statutes.”).

⁵³ *Id.* at 84.

with tax-exempt status under § 501(c)(3).⁵⁴ More precisely, “nondiscriminatory practices and policies comport with the commonly accepted notion of being ‘charitable’ and conferring public benefit.”⁵⁵ Although an organization that discriminates would lose its § 501(c)(3) tax exemption under the proposal, it may still qualify for tax exemption under § 501(c)(4) as a “social welfare organization.”⁵⁶ However, social welfare organizations do not qualify for the § 170 charitable contributions deduction,⁵⁷ thereby preventing offending organizations from using tax-deductible donations that they receive to discriminate against members of society.⁵⁸

Nevertheless, applying a nondiscrimination requirement to religious organizations is perplexing because federal income tax law does not define “religious” or “religion” due primarily to First Amendment concerns.⁵⁹ Because the IRS is acutely aware of the constitutional minefield surrounding any attempt to define “religion” or “religious,” or “church,” it therefore opts for a broad interpretation.⁶⁰ For federal income tax law purposes, religious organizations are generally defined more broadly than “churches” or “houses of worship,” and can include schools and universities, social service agencies, publishers, broadcasters, and cemeteries.⁶¹ However, with respect to churches, some designation is necessary because of the unique treatment and protection the Code accords to “churches, their integrated auxiliaries, and conventions or associations of churches.”⁶² As proposed in my prior article, churches should be excepted

⁵⁴ *Id.* at 84–85.

⁵⁵ *Id.* at 85.

⁵⁶ *Id.* at 88; *see, e.g.,* *Regan v. Taxation with Representation of Wash.*, 461 U.S. 540, 544 (1983) (discussing the availability of tax exemption as a social welfare organization); *Branch Ministries v. Rossotti*, 211 F.3d 137, 143 (D.C. Cir. 2000) (discussing the Church’s ability to form a related organization under 501(c)(4)). Section 501(c)(4) grants tax-exempt status to [c]ivic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

I.R.C. § 501(c)(4)(A) (2000).

⁵⁷ *Mirkay, Charities & Discrimination*, *supra* note 5, at 88; *see* I.R.C. § 170(a)(1), (c)(1)–(2) (2000).

⁵⁸ *Mirkay, Charities & Discrimination*, *supra* note 5, at 88.

⁵⁹ *See* HOPKINS, *supra* note 48, § 10.2(a) (reviewing various Supreme Court and state court language grappling with defining religion).

⁶⁰ JAMES J. FISHMAN & STEPHEN SCHWARZ, *NONPROFIT ORGANIZATIONS: CASES AND MATERIALS* 444 (3d ed. 2006); *see also* HOPKINS, *supra* note 48, § 10.3 (stating the IRS has resisted publishing criteria for what constitutes a church).

⁶¹ FISHMAN & SCHWARZ, *supra* note 60, at 445.

⁶² I.R.C. § 508(c)(1)(A) (2000); *see also* I.R.C. § 508(b) (exempting churches from notice rules governing other exempt organizations); I.R.C. § 6033(a)(2)(A)(iii) (exempting religious orders from filing certain annual returns); I.R.C. § 7611 (restricting auditing of churches);

from the nondiscrimination requirement due to First Amendment concerns.⁶³ This raises the issue of how narrowly the federal income tax definition of a “church” should be drawn, taking into consideration that schools, universities, and social service agencies may presently be component parts of a church or qualify as “integrated auxiliaries” and, thus, treated as churches under the Code.⁶⁴ Although my prior article briefly addressed the difficulty of applying a nondiscrimination requirement to religious organizations, it acknowledged the necessity of additional and more thorough discussion on the issue;⁶⁵ thus, the focus of this Article.

Accordingly, this Article examines the propriety and constitutionality of subjecting religious organizations to a § 501(c)(3) nondiscrimination requirement and crafting a more narrow church exception to that requirement. This Article ultimately proposes modification of the current statutory and regulatory exemption scheme for religious organizations to effect a more narrowly drawn federal income tax definition of a church. Part I of this Article provides a statutory and regulatory framework for the proposal. Part II briefly reviews other noteworthy proposals with respect to combating discrimination, such as expansion of the public-policy doctrine and broader applicability of civil rights laws, and concludes that both fail in the context of sexual orientation and marital status discrimination. It further offers a potential solution in the form of statutory and regulatory amendments that would narrow the eligibility of integrated auxiliary status and, thus, limit the availability of church tax benefits to affiliated organizations. Part III attempts to tackle the seemingly enormous, yet precarious, constitutional issues inherent in the proposal; namely, First Amendment free speech, establishment, and free exercise concerns.

I. THE EVOLVING TAXONOMY OF “RELIGIOUS” AND “CHURCH”

A. Overview of the Federal Income Tax Exemption⁶⁶

In order to discuss the incongruity of deeming a discriminatory organization “religious,” it is necessary to understand the exemption statute and the regulatory tests that must be satisfied before the IRS grants an exemption. Section 501(c)(3) provides for the federal income tax exemption of nonprofit corporations and certain other entities

infra notes 101–05 and accompanying text.

⁶³ Mirkay, *Charities & Discrimination*, *supra* note 5, at 100. The article further proposed extending the exception to religious orders and similar exclusively religious organizations exempt under § 501(c)(3). *Id.* at 100 n.325.

⁶⁴ *Id.* at 98–100.

⁶⁵ *Id.* at 88 (discussing the difficulties of applying a nondiscrimination requirement to religious organizations).

⁶⁶ The discussion in this subpart is substantially similar to a corresponding discussion contained in Mirkay, *Charities & Discrimination*, *supra* note 5, at 54–56.

organized and operated exclusively for religious, charitable, scientific, . . . or educational purposes, . . . no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation . . . and which does not participate in, or intervene in . . . any political campaign on behalf of (or in opposition to) any candidate for public office.⁶⁷

The principal benefit of a § 501(c)(3) exemption is that the exempt organization is entitled to receive charitable contributions that are tax-deductible to its donors under § 170(a)(1).⁶⁸ For the most part, only organizations exempt under § 501(c)(3) are eligible for this valuable benefit.⁶⁹ In addition, organizations exempt under § 501(c)(3) are also eligible to issue bonds, subject to certain limitations, the interest on which is not included in the bondholder's income.⁷⁰

IRS regulations and rulings define the meaning of each of the eight specific exempt purposes listed in the statute (for example, religious, charitable,⁷¹ and educational).⁷² Section 501(c)(3) establishes both an organizational test and an operational test for determining whether an organization fulfills its exempt purposes;⁷³ to qualify for exemption, an organization must meet both tests.⁷⁴ The organizational

⁶⁷ I.R.C. § 501(c)(3) (2000). Specifically, § 501(a) provides that "[a]n organization described in subsection (c) or (d) . . . shall be exempt from taxation under this subtitle. . . ." *Id.* § 501(a).

⁶⁸ *Id.* § 170(a)(1) ("There shall be allowed as a deduction any charitable contribution . . . payment of which is made within the taxable year."). Donors must primarily make contributions to either governmental entities or charitable organizations under § 501(c)(3). *See id.* § 170(c)(1)–(2).

⁶⁹ Certain veterans' organizations, fraternal organizations, and cemetery organizations, which are exempt from federal income tax under other subsections of § 501(c), are also entitled to receive tax-deductible contributions. *See id.* § 170(c)(3)–(5).

⁷⁰ *See id.* §§ 103(a), 141, 145–49.

⁷¹ *See supra* note 50; *see also* Mirkay, *Charities & Discrimination*, *supra* note 5 (discussing the meaning of "charitable" under § 501(c)(3) and the common practice of collectively referring to the entities listed in the statute as "charitable"). In addition, the IRS has determined that other qualifying purposes meet the overall public-benefit principle of § 501(c)(3) based on an expansive interpretation of "charitable." *See* Brennen, *Tax Expenditures*, *supra* note 41, at 178.

⁷² Treas. Reg. § 1.501(c)(3)-1(d) (as amended in 2008) (categorizing the exemptions as: religious, charitable, scientific, testing for public safety, literary, educational, or prevention of cruelty to children or animals). Section 501(c)(3) lists as an eighth exempt purpose "to foster national or international amateur sports competition," which is not addressed by any regulation. I.R.C. § 501(c)(3) (2000).

⁷³ I.R.C. § 501(c)(3).

⁷⁴ Treas. Reg. § 1.501(c)(3)-1(a)(1) (as amended in 2008).

test relates solely to the language used in the organization's governing documents.⁷⁵ An organization meets the requirements of the test if it was organized exclusively for at least one tax-exempt, charitable purpose.⁷⁶ This is possible only if the organizing document (1) limits the organization's purpose to one or more exempt purposes, and (2) does not expressly empower it to substantially engage in activities that do not further any exempt purposes.⁷⁷ The organizational test also imposes requirements on the distribution of the organization's assets upon dissolution.⁷⁸

The purpose of the operational test is to ensure that an exempt organization's resources and activities are devoted primarily to its exempt purposes. The regulations break down the operational test into two components: (1) the primary-purpose-or-activity test and (2) the private-inurement prohibition.⁷⁹ Under the primary-purpose-or-activity test, "[a]n organization will be regarded as *operated exclusively* for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3)."⁸⁰ An organization will not pass this test if "more than an insubstantial part of its activities is not in furtherance of an exempt purpose."⁸¹

Under the private-inurement prohibition, an organization will not satisfy the operational test "if its net earnings inure in whole or in part to the benefit of private shareholders or individuals."⁸² The regulations define the term "private shareholder or individual" as "persons having a personal and private interest in the activities of the organization,"⁸³ such as officers, directors, or other individuals in a position to assert influence or control over the organization's operations and activities.⁸⁴ The prohibition is absolute—any amount of inurement is impermissible.⁸⁵ Organizations exempt under § 501(c)(3) are also subject to other statutory and regulatory standards with respect to their operations, including the private-benefit doctrine.⁸⁶

⁷⁵ See *id.* § 1.501(c)(3)-1(b)(1)(i).

⁷⁶ See *id.* § 1.501(c)(3)-1(a)(1).

⁷⁷ *Id.* § 1.501(c)(3)-1(b)(1)(i).

⁷⁸ See *id.* § 1.501(c)(3)-1(b)(4). The IRS typically implements this regulation by requiring an organization, either in its governing document or under relevant state law, to explicitly dedicate its assets to one or more exempt purposes in the event of dissolution. *Id.*

⁷⁹ See *id.* § 1.501(c)(3)-1(c)(1) & (2).

⁸⁰ *Id.* § 1.501(c)(3)-1(c)(1).

⁸¹ *Id.*

⁸² *Id.* § 1.501(c)(3)-1(c)(2).

⁸³ *Id.* § 1.501(a)-1(c); see also I.R.S. Gen. Couns. Mem. 39,862 (Nov. 22, 1991) ("The proscription against inurement generally applies to . . . persons who, because of their particular relationship with an organization, have an opportunity to control or influence its activities.").

⁸⁴ See HOPKINS, *supra* note 48, § 20.3.

⁸⁵ See Treas. Reg. § 1.501(c)(3)-1(c)(2) (as amended in 2008).

⁸⁶ See *id.* § 1.501(c)(3)-1(d)(1)(ii). For further discussion of the private-benefit doctrine and other operational restrictions, see Nicholas A. Mirkay, *Relinquish Control! Why the IRS Should Change Its Stance on Exempt Organizations in Ancillary Joint Ventures*, 6 NEV. L.J. 21, 30–34, 62 (2005).

As previously mentioned, the Supreme Court's *Bob Jones University* decision imposes the additional, nonstatutory public-policy doctrine on an organization seeking tax-exempt status under § 501(c)(3).⁸⁷ By failing to articulate a clearly defined source of "established public policy,"⁸⁸ courts have left the doctrine open to the IRS's unfettered discretion,⁸⁹ potentially allowing discrimination to flourish in areas other than race, civil disobedience, and illegality.

B. "Religious" Organization and "Church" under Federal Income Tax Law

1. Definition of "Religious" and "Church"⁹⁰

To allay any constitutional concerns, religious organizations are generally defined broadly to include a variety of other organizations in addition to churches or traditional houses of worship.⁹¹ The IRS is acutely aware of the constitutional ramifications of attempting to define "religion" or "religious" narrowly, and has advised its agents to interpret the terms broadly to encompass "even those sects that do not believe in a Supreme Being."⁹² Accordingly, the IRS has subscribed to this general rule: "in the absence of a clear showing that the beliefs or doctrines under consideration are not sincerely held by those professing or claiming them as a religion, the Service cannot question the 'religious' nature of those beliefs."⁹³ The IRS concluded that this rule comports with the Establishment Clause: "An attempt to define religion, even for purposes of statutory construction, violates the 'establishment' clause since it necessarily delineates and, therefore, limits what can and cannot be a religion."⁹⁴ In fact, the IRS has typically denied religious organization exemptions only on other grounds, such as the private-inurement prohibition⁹⁵ or the restrictions on lobbying and political campaign activities under § 501(c)(3).⁹⁶

⁸⁷ *Bob Jones Univ. v. United States*, 461 U.S. 574, 585 (1983).

⁸⁸ *Id.* at 586.

⁸⁹ See Brennen, *Tax Expenditures*, *supra* note 41, at 178 n.48.

⁹⁰ Portions of the discussion in this subpart are substantially similar to a corresponding discussion contained in Mirkay, *Charities & Discrimination*, *supra* note 5, at 95–99.

⁹¹ See *supra* notes 60–61 and accompanying text.

⁹² FISHMAN & SCHWARZ, *supra* note 60, at 445; see also I.R.S. Gen. Couns. Mem. 36,993 (Feb. 3, 1977) (finding that a witches' coven qualified as a church under § 501(c)(3)).

⁹³ I.R.S. Gen. Couns. Mem. 36,993 (Feb. 3, 1977); see also *Holy Spirit Ass'n for the Unification of World Christianity v. Tax Comm'n*, 435 N.E.2d 662, 668 (N.Y. 1982) ("It is for religious bodies themselves, rather than the courts or administrative agencies, to define, by their teachings and activities, what their religion is. The courts are obliged to accept such characterization . . . unless it is found to be insincere or [a] sham.").

⁹⁴ I.R.S. Gen. Couns. Mem. 36,993 (Feb. 3, 1977).

⁹⁵ See *supra* notes 82–86 and accompanying text.

⁹⁶ See, e.g., *Branch Ministries v. Rossotti*, 211 F.3d 137 (D.C. Cir. 2000) (addressing a church's political campaign prohibition violation); *Christian Echoes Nat'l Ministry, Inc. v.*

Even though it cannot question or regulate religious belief and opinions, Congress can regulate religious action and practices.⁹⁷ In *Reynolds v. United States*, the Supreme Court upheld a federal law criminalizing the practice of polygamy.⁹⁸ In holding that citizens were not excepted from the statute because of their religious beliefs, the Court explained that a law may impede religious practices, but not religious beliefs or opinions.⁹⁹ In a subsequent case involving a state statute that regulated solicitation by charitable organizations, the Court elaborated on *Reynolds* by stating that “the [First] Amendment embraces two concepts—freedom to believe and freedom to act. The first is absolute but, in the nature of things, the second cannot be. Conduct remains subject to regulation for the protection of society.”¹⁰⁰

Although the same congressional and IRS trepidation with respect to religious belief is present in attempting to define a “church,”¹⁰¹ some designation is necessary because of the unique treatment and protection that churches receive under the Code.¹⁰² As one court astutely observed, “To exempt churches, one must know what a church is.”¹⁰³ In making these designations, the IRS follows a fifteen-item checklist¹⁰⁴—including a distinct legal existence, a recognized creed and form of worship,

United States, 470 F.2d 849 (10th Cir. 1972), *cert. denied*, 414 U.S. 864 (1973) (involving the revocation of an organization’s exempt status because it failed to meet the operational test and violated lobbying and political campaign restrictions); *Unitary Mission Church of Long Island v. Comm’r*, 74 T.C. 507 (1980), *aff’d*, 647 F.2d 163 (2d Cir. 1981) (upholding the denial of a church’s exemption because of the private benefit and inurement to the organization’s controlling members); *see also* *United States v. Kuch*, 288 F. Supp. 439, 444 (D.D.C. 1968) (determining that the organization at issue was not “religious” because it was clearly motivated by the “desire to use drugs and to enjoy drugs for their own sake”).

⁹⁷ FISHMAN & SCHWARZ, *supra* note 60, at 453.

⁹⁸ 98 U.S. 145 (1878).

⁹⁹ *Id.* at 166.

¹⁰⁰ *Cantwell v. Connecticut*, 310 U.S. 296, 303–04 (1940). At issue in the case was a state statute that prohibited the solicitation of contributions by religious, charitable, or philanthropic causes without obtaining official approval. *Id.* at 301–02. The Court ultimately concluded that such approval constituted an invalid prior constraint on the free exercise of religion. *Id.* at 307.

¹⁰¹ HOPKINS, *supra* note 48, § 10.3.

¹⁰² *See infra* notes 111–16 and accompanying text.

¹⁰³ *De La Salle Inst. v. United States*, 195 F. Supp. 891, 903 (N.D. Cal. 1961). The court’s full observation states that: “Congress must either define ‘church’ or leave the definition to the common meaning and usage of the word; otherwise, Congress would be unable to exempt churches.” *Id.*

¹⁰⁴ ROBERT LOUTHIAN & THOMAS MILLER, I.R.S., *DEFINING “CHURCH”—THE CONCEPT OF A CONGREGATION* 2 (1993), <http://www.irs.gov/pub/irs-tege/eotopica94.pdf>. The fifteen points are as follows:

- (a) a distinct legal existence, (b) a recognized creed and form of worship,
- (c) a definite and distinct ecclesiastical government, (d) a formal code of doctrine and discipline, (e) a distinct religious history, (f) a membership not associated with any other church or denomination, (g) an organization of ordained ministers, (h) ordained ministers selected after completing

a formal code of doctrine and discipline, a distinct religious history, and the selection of ordained ministers after prescribed studies.¹⁰⁵ Although the IRS has cautioned that these criteria are not exclusive and that it ultimately uses a facts-and-circumstances determination,¹⁰⁶ the criterion that courts most consistently rely on in determining the existence of a church is the presence or absence of an established and regular congregation.¹⁰⁷ Specifically, the focus is on a coherent and dynamic membership with shared religious purposes and beliefs.¹⁰⁸ The size of the congregation is not determinative.¹⁰⁹ Because charitable organizations must primarily confer public benefit, the congregational or associational facet of a church comports with that requirement.¹¹⁰

Although nearly all religious organizations are eligible for a tax exemption under § 501(c)(3), only “churches, their integrated auxiliaries, and conventions or associations of churches” are presumed not to be private foundations,¹¹¹ and thus, excepted from the notice requirements of § 508.¹¹² That is, a church does not need to file an application for the IRS to recognize it as exempt under § 501(c)(3).¹¹³ Churches are also relieved of filing annual information returns with the IRS.¹¹⁴ In addition, the Code confers upon churches special procedural safeguards with respect to IRS

prescribed studies, (i) a literature of its own, (j) established places of worship, (k) regular congregations, (l) regular religious services, (m) Sunday schools for religious instruction of the young, (n) schools for the preparation of its ministers, and (o) any other facts and circumstances that may bear upon the organization’s claim for church status.

Id. In instructing that the criteria “are not exclusive and are not to be mechanically applied,” the IRS Chief Counsel recommended the addition of the fifteenth criterion. *See* I.R.S. Gen. Couns. Mem. 38,982 (May 3, 1983). Federal courts adopted the original fourteen-point test in *Am. Guidance Found., Inc. v. United States*, 490 F. Supp. 304, 306 n.2 (D.D.C. 1980) (not including the residual, “facts and circumstances” factor).

¹⁰⁵ LOUTHIAN & MILLER, *supra* note 104.

¹⁰⁶ *Id.*

¹⁰⁷ *Id.* at 3 (“At a minimum, a church includes a body of believers or communicants that assembles regularly in order to worship.” (quoting *Am. Guidance Found.*, 490 F. Supp. at 306)).

¹⁰⁸ LOUTHIAN & MILLER, *supra* note 104, at 8.

¹⁰⁹ *See id.*

¹¹⁰ Wendy Gerzog Shaller, *Churches and Their Enviably Tax Status*, 51 U. PITT. L. REV. 345, 351, 353 n.52; *see also* Charles M. Whelan, “Church” in the Internal Revenue Code: The Definitional Problems, 45 FORDHAM L. REV. 885, 926 (1977) (discussing the centrality of the congregational model to the I.R.S.’s conception of a “church”).

¹¹¹ I.R.C. § 508(b), (c)(1)(A) (2000). *See infra* note 148 for an explanation of private foundation versus public charity status under § 509.

¹¹² *See id.* § 508(c)(1).

¹¹³ *See id.* § 508(c)(1)(A); Treas. Reg. § 1.508-1(a)(3)(i)(a) (as amended in 1995).

¹¹⁴ *See* I.R.C. § 6033(a)(2)(A)(I) (2000). However, churches are required to file a Form 990-T, Exempt Organization Business Income Tax Return, reporting any income that is subject to the unrelated business income tax imposed by § 511(a). *See also* Treas. Reg. § 1.6012-2(e) (as amended in 2007).

examinations or audits.¹¹⁵ Moreover, among other exemptions, churches are exempted from certain rules governing qualified retirement plans, and social security, self-employment, and withholding taxes.¹¹⁶

As illustrated below, churches have varying and multifaceted structures, and their activities typically comprise more than just providing religious services and worship to their congregants. Many churches also operate schools, seminaries, or social-service agencies. The manner in which the church operates these other activities—within or without a separate legal entity—raises potential tax exemption issues.¹¹⁷ Until a church places an activity in a separate legal entity, the IRS generally considers it to be a part of the church and therefore covered by the church's exemption.¹¹⁸ Once the church forms a new legal entity to conduct an activity, the entity must obtain its own tax-exempt status.¹¹⁹ Due to the entity's relationship to the church, the Code typically classifies it as an "integrated auxiliary," which accords the entity church-like treatment.¹²⁰ The statutory requirements and significance of being categorized as an integrated auxiliary are discussed in greater detail in the following subparts.

2. Historical Overview of the Distinction

The history of the Code's distinction between churches and religious organizations is particularly relevant to this Article. Primarily, it exposes Congress's choice to treat churches differently from other religious organizations, and how that special treatment was extended to integrated auxiliaries or affiliates of churches, such as educational institutions. As this discussion reveals, this extension of church-like treatment directly impacts the applicability of a nondiscrimination requirement to these church affiliates.

The tax exemption of religious organizations—specifically, churches—is deep-rooted in American history.¹²¹ Beginning in 1798, Congress recognized the propriety

¹¹⁵ See I.R.C. § 7611 (2000). Section 7611(h)(1) defines church as "any organization claiming to be a church" and "any convention or association of churches." *Id.*

¹¹⁶ NICHOLAS P. CAFARDI & JACLYN FABEAN CHERRY, UNDERSTANDING NONPROFIT AND TAX EXEMPT ORGANIZATIONS § 8.03[C] (2006) (citing I.R.C. §§ 410(c)(1)(B), 411(e)(1)(B), 412(h)(4), 414(e), 1402(e), 3121(b)(8), 3401(a)(9)); see also Whelan, *supra* note 110, at 887–89 & nn.11–25 (listing fifteen basic religious distinctions recognized by the Internal Revenue Code).

¹¹⁷ CAFARDI & CHERRY, *supra* note 116, § 8.06.

¹¹⁸ *Id.*

¹¹⁹ *Id.*

¹²⁰ *Id.*

¹²¹ *Walz v. Tax Comm'n of N.Y.*, 397 U.S. 664, 676–77 (1970); see JOHN D. COLOMBO & MARK A. HALL, THE CHARITABLE TAX EXEMPTION 226 (1995) ("[T]he core rationale for religious exemption has seldom been questioned."); Edward McGlynn Gaffney, Jr., *Exemption of Religious Organizations from Federal Taxation*, in RELIGIOUS ORGANIZATIONS IN THE UNITED STATES 409, 411 (James A. Serritella et al. eds., 2006) [hereinafter Gaffney, *Federal*

of, and adopted for federal tax purposes, the states' exemptions of churches from real estate tax and other direct taxes.¹²² Since the Sixteenth Amendment's enactment, religious organizations have been continuously exempted from federal income tax.¹²³ In 1917, Congress further extended religious organizations' federal tax benefits by enacting a deduction for contributions made to "corporations or associations organized and operated exclusively for religious, charitable, scientific, or educational purposes."¹²⁴ Although churches are considered to be religious organizations, the opposite is not generally correct.¹²⁵

The statutory distinction between churches and religious organizations primarily began with the enactment of the unrelated business income tax in 1950.¹²⁶ By specifically excepting "a church, a convention or association of churches" from the new tax,¹²⁷ Congress acknowledged the difference between churches (religious organizations that maintain "exclusively religious activities") and church-affiliated entities ("religious organizations that carry on charitable, literary, or educational activities").¹²⁸ As a consequence, church-related charitable and educational entities, such as colleges and universities, social service agencies, and hospitals, appeared to be subject to the new tax.¹²⁹ Because of the varying and multifaceted structure of American churches, however, the IRS experienced great difficulty in implementing this distinction.¹³⁰ As explained by one legal scholar, American churches are generally either "congregational" or "hierarchical" in their configuration:

In the congregational churches, the faith and internal religious law of the denominations make each local congregation

Taxation] ("The U.S. federal government and all fifty states maintain a system of general exemption of religion from the payment of most forms of taxation. This widespread American practice is not a recent invention; on the contrary, it is rooted deeply in the principle of religious freedom, a value at the very core of the American constitutional order.").

¹²² *Walz*, 397 U.S. at 677-78 & n.5; see also Daniel M. Andersen, *Political Silence at Church: The Empty Threat of Removing Tax-Exempt Status for Insubstantial Attempts to Influence Legislation*, 2006 BYU L. REV. 115, 122 ("[B]y traditional default, churches are generally not part of the federal tax base.").

¹²³ *Walz*, 397 U.S. at 676 n.4.

¹²⁴ War Revenue Act of 1917, ch. 63, § 1201(2), 40 Stat. 300, 330; see also Aprill, *supra* note 6, at 848.

¹²⁵ Shaller, *supra* note 110, at 350.

¹²⁶ Whelan, *supra* note 110, at 901.

¹²⁷ Revenue Act of 1950, ch. 994, § 421(b)(1), 64 Stat. 948, 948; see also Whelan, *supra* note 110, at 902. The exception was eliminated by the Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 536 (codified at I.R.C. § 511).

¹²⁸ Reka Potgieter Hoff, *The Financial Accountability of Churches for Federal Income Tax Purposes: Establishment or Free Exercise?*, 11 VA. TAX REV. 71, 82 (1991).

¹²⁹ Whelan, *supra* note 110, at 902-03.

¹³⁰ *Id.* at 903.

autonomous. The coordination of the various congregations' activities is a matter of voluntary agreement or "covenant." Each local congregation is usually a separate civil law corporation or trust. . . . Thus there is no Baptist Church; there are only Baptist churches and Baptist conventions or associations of churches. . . . In the hierarchical churches, such as the Roman Catholic, Presbyterian, Eastern Orthodox, and Mormon denominations, the faith and internal religious law create a single church authority with jurisdiction over all the members and branches of the church. Local congregations are divisions, not autonomous units. Thus it is entirely proper to speak of the "Roman Catholic Church" or the "Mormon Church."¹³¹

Regardless of their structure, churches uniformly utilize numerous corporations and trusts to accomplish their various missions.¹³² For instance, the Roman Catholic Church in the United States does not technically exist as a single entity but rather as "a conglomeration . . . of distinct taxable entities united in religious faith, worship and authority but not in civil law identity or control."¹³³ Accordingly, in implementing this exception with respect to various American churches, the IRS had to determine which entities comprised the "church" and which merely constituted church-related entities not covered by the statutory exception.¹³⁴

Although the Tax Reform Act of 1969 (1969 Act) eliminated the church exception to the unrelated business income tax,¹³⁵ the distinction between churches and religious organizations was incorporated into newly enacted code provisions. The 1969 Act added the notice requirement of § 508 to the Code, requiring newly created nonprofit

¹³¹ *Id.* at 903–04; see Hoff, *supra* note 128, at 83 (noting that under a congregational structure, church property is owned in trust by a group of lay trustees, whereas in a hierarchical structure, church property is held by a bishop "as a corporation sole").

¹³² Whelan, *supra* note 110, at 904.

¹³³ *Id.* at 905. Although the IRS issues a "group ruling" to the United States Catholic Conference, which effectively permits the IRS to deal with the Roman Catholic church as a single "unit," the ruling does acknowledge that the church is comprised of many separate and distinct entities as listed and updated annually in the Official Catholic Directory. *Id.* at 905 n.86.

¹³⁴ *Id.* at 905. Whelan further identified the classification problem raised with respect to "religious orders" within the Roman Catholic Church. *Id.*; see, e.g., *De La Salle Inst. v. United States*, 195 F. Supp. 891 (N.D. Cal. 1961). The IRS finally addressed the issue by regulation. See Treas. Reg. § 1.511-2(a)(3), T.D. 6301, 1958-2 C.B. 222–23 (including a religious order within the meaning of "church" if the order is (i) an integral part of the church, and (ii) engaged in implementing the church's functions, regardless of whether it is separately incorporated).

¹³⁵ Tax Reform Act of 1969, Pub. L. No. 91-172, § 121, 83 Stat. 487, 536–37 (codified as amended at 26 U.S.C. §§ 501–526). Under the Act, all § 501(a) tax-exempt organizations are subject to the unrelated business income tax except for federal instrumentalities. *Id.*

organizations to file an application with the IRS to be recognized as exempt from federal income tax under § 501(c)(3).¹³⁶ However, "churches, their integrated auxiliaries, and conventions or associations of churches" were specifically exempted from this new notice requirement.¹³⁷ As discussed below, Congress used the same language for purposes of exemption from the § 6033 annual return requirement.¹³⁸ The new "integrated auxiliaries" language resulted from compromise negotiations between the Senate Finance Committee, the Joint Committee on Taxation, and American churches' representatives concerned about the restrictive and administratively difficult language utilized to except churches from the unrelated business income tax.¹³⁹ Although the Senate Finance Committee's report did not define the new term, it did provide some examples of integrated auxiliaries, including "mission societies and the church's religious schools, youth groups, and men's and women's organizations."¹⁴⁰ The 1969 Act also broadened the exemption from the annual return requirement to include the "exclusively religious activities of any religious order."¹⁴¹

Prior to its amendment in the 1969 Act, § 6033 exempted all religious organizations from the requirement to file annual information returns with the IRS.¹⁴² The 1969 Act, however, limited this religious exception to just "churches, their integrated auxiliaries, and conventions or associations of churches."¹⁴³ In proposed regulations

¹³⁶ I.R.C. § 508(a) (2000).

¹³⁷ Tax Reform Act of 1969, Pub. L. No. 91-172, § 101, 83 Stat. 487, 494-96 (codified at I.R.C. § 508(c)(1)(A) (2000)).

¹³⁸ See *infra* note 142 and accompanying text.

¹³⁹ Whelan, *supra* note 110, at 914-15.

¹⁴⁰ S. REP. NO. 91-552, at 52 (1969). The House conference committee report essentially adopted the language of this Senate report: "The integrated auxiliary organizations to which this applies include the church's religious school, youth group, and men's and women's clubs." H.R. REP. NO. 91-782, at 286 (1969); see also Whelan, *supra* note 110, at 915-16.

¹⁴¹ I.R.C. § 6033(a)(2)(A)(iii) (2000). The House conference committee report explains that the term "exclusively religious activities" does not include "any educational, charitable, or other exempt activities which would serve as a basis of exemption under section 501(c)(3) if an organization which is not a religious organization is required to report with respect to such activities." H.R. REP. NO. 91-782, at 286 (1969); see also Whelan, *supra* note 110, at 916. There is no documented IRS effort requiring religious orders to report on non-"exclusively religious" activities. *Id.*

¹⁴² Specifically, § 6033 then provided that

[n]o such annual return need be filed under this subsection by any organization exempt from taxation under the provisions of section 501(a)-(1) which is a religious organization described in section 501(c)(3); or . . . (4) which is an organization described in section 501(c)(3), if such organization is operated, supervised, or controlled by or in connection with a religious organization described in paragraph (1).

I.R.C. § 6033(a) (1954).

¹⁴³ See Tax Reform Act of 1969, Pub. L. No. 91-172, § 101, 83 Stat. 487, 519-23; I.R.C. § 6033(a)(1) (1954). Paragraph (2) of § 6033(a) was redesignated as paragraph (3) by the Tax

released in 1976, the Treasury Department defined “integrated auxiliary” as a § 501(c)(3) organization whose primary purpose is “to carry out the tenets, functions, and principles of faith of the church with which it is affiliated” and whose operations “directly promote religious activity among the members of the church.”¹⁴⁴ The proposed regulation provided examples similar to those espoused in the Senate Finance Committee report, but additionally stated that “[s]chools of a general academic or vocational nature are not considered to be integrated auxiliaries, even though they have a religious environment or promote the church’s teaching.”¹⁴⁵ Consistent with this statement, the proposed regulations used a parochial elementary school as an example of an organization that was not an integrated auxiliary. The regulation explained that the school’s primary purpose was to fulfill educational needs, even though it included religious services and subjects in its academic programs. Thus, the school failed the “purpose and function” test of the regulation.¹⁴⁶ American churches of all faiths and denominations almost unanimously rejected this test, claiming that it represented IRS intrusion into their religious activities.¹⁴⁷

In the Tax Reform Act of 1976, Congress enacted § 501(h), which created an expenditure-based safe harbor for certain publicly funded charitable organizations—“public charities”¹⁴⁸—with respect to their lobbying activities.¹⁴⁹ Pursuant to § 501(h)(5), churches, their integrated auxiliaries, and a convention or association of churches are ineligible to make this election.¹⁵⁰ Because the IRS had recently

Increase Prevention and Reconciliation Act of 2005, Pub. L. No. 109-222, 120 Stat. 345 (codified at I.R.C. § 6033(a)(3)(A)(i) (2006)).

¹⁴⁴ Prop. Treas. Reg. § 1.6033-2(g)(5)(i), 41 Fed. Reg. 6073 (Feb. 11, 1976).

¹⁴⁵ *Id.*

¹⁴⁶ *Id.* § 1.6033-2(g)(5), example (3); *see also* Whelan, *supra* note 110, at 894–95. Because example (3) in the proposed regulations specifically provided that the school had a separate legal identity from the church, it raised the issue of whether an organization must be legally separate from the church (i.e., a corporation, trust, or other entity) in order to qualify as an integrated auxiliary. The question was, and continues to be, relevant in that many churches directly own and operate schools, hospitals, and other social service agencies without separate legal entities for such operations. *See id.* at 894 n.56.

¹⁴⁷ *See* Whelan, *supra* note 110, at 895; *see also* Hoff, *supra* note 128, at 89 n.92.

¹⁴⁸ An organization that meets the requirements of § 501(c)(3) is classified as either a “public charity” or a “private foundation.” I.R.C. § 509(a)(1)–(3) (2000). A “public charity” typically receives its income from a broader segment of the general public in the form of gifts, contributions, or receipts from the performance of services, whereas a “private foundation” typically receives contributions from only a few individuals or entities. FISHMAN & SCHWARZ, *supra* note 60, at 751. Furthermore, private foundations are subject to additional excise taxes. *See* I.R.C. §§ 4940–4945 (2000).

¹⁴⁹ Tax Reform Act of 1976, Pub. L. No. 94-455, 90 Stat. 1520, 1720 (codified as amended in scattered sections of 26 U.S.C.).

¹⁵⁰ *See* Tax Reform Act of 1969, Pub. L. No. 91-172, § 101, 83 Stat. 487, 519–23; I.R.C. § 501(h)(5) (2000). Section 501(h)(5) also excludes members of an “affiliated group of organizations” if one of the members is a church, an integrated auxiliary thereof, or a convention

released its proposed regulations on “integrated auxiliaries” under § 6033, Congress used the enactment of § 501(h) and its use of that language as an opportune time to comment on the regulations’ interpretation of the statutory term.¹⁵¹ Specifically, the House Ways and Means Committee inserted the following comment into its report accompanying the § 501(h) legislation:

Because proposed regulations have recently been published regarding the meaning of the term “integrated auxiliary” and because that term is used in this bill, your committee wishes to make it clear—in agreement with the conclusions of the proposed regulations—that theological seminaries, religious youth organizations, and men’s fellowship associations which are associated with churches would generally constitute integrated auxiliaries. Your committee also intends (in agreement with the conclusions in the proposed regulations) that hospitals, elementary grade schools, orphanages, and old-age homes are organizations which frequently are established without regard to church relationships and are to be treated for these purposes the same as corresponding secular charitable, etc., organizations[;] that is, such entities are not to be regarded as “integrated auxiliaries.”¹⁵²

The Senate Finance Committee report did not include this language, or any other language, explaining the meaning of “integrated auxiliaries.”¹⁵³ The House conference committee report followed the Senate report, explicitly adopting a “no position” standpoint with respect to the above-quoted House report language.¹⁵⁴ Thus, as one legal scholar noted, the controversy over integrated auxiliaries ended without a victor—the churches failed to convince the conference committee to condemn the proposed regulations under § 6033, and the IRS failed to obtain legislative history favoring its restrictive regulatory definition.¹⁵⁵

In 1977, the IRS issued final regulations under § 6033 that attempted to resolve some of the controversies surrounding the proposed regulations.¹⁵⁶ First, to be an integrated auxiliary of a church, the final regulations required that a church-affiliated organization must be a separate legal entity that is tax-exempt under § 501(c)(3).¹⁵⁷

or association of churches. *Id.*; see also I.R.C. § 4911(f)(2) (2000) for a definition of “affiliated group[s] of organizations.”

¹⁵¹ Whelan, *supra* note 110, at 920.

¹⁵² H.R. REP. NO. 94-1210, at 15–16 (1976); see also Whelan, *supra* note 110, at 920.

¹⁵³ S. REP. NO. 94-938, pt. 2, at 79 (1976); see also Whelan, *supra* note 110, at 921.

¹⁵⁴ H.R. REP. NO. 94-1515, at 533–34 (1976); see also Whelan, *supra* note 110, at 921.

¹⁵⁵ Whelan, *supra* note 110, at 921.

¹⁵⁶ Treas. Reg. § 1.6033-2(g) (1977).

¹⁵⁷ *Id.* § 1.6033-2(g)(5)(i)(a); see *id.* at example (6).

Second, the final regulations disposed of the “purpose and function” test in favor of a new “principal activity” test: the organization’s principal activity must be “exclusively religious.”¹⁵⁸ An “exclusively religious” activity was one that would qualify for § 501(c)(3) tax-exempt status as a religious organization if it applied for its own exemption.¹⁵⁹ Accordingly, a church-affiliated elementary school was not accorded an integrated auxiliary exemption under the regulations because its principal activity was educational rather than religious.¹⁶⁰ Notwithstanding this distinction, the final regulations explicitly excepted a church-affiliated elementary or secondary school from filing an annual return on another basis—the Treasury Secretary’s statutorily granted discretionary power.¹⁶¹

American churches objected to the “exclusively religious” standard in the regulations, resulting in litigation.¹⁶² While that litigation was pending, Congress enacted § 3121(w) that set forth a financial support requirement for church-affiliated organizations desiring to elect out of social security coverage.¹⁶³ This legislative development prompted the IRS to issue Revenue Procedure 86-23, which abandoned the “exclusively religious” activity test in exchange for a more neutrally applied “internal support test.”¹⁶⁴ This test is satisfied if the affiliated organization either (I) does not offer

¹⁵⁸ *Id.* § 1.6033-2(g)(5)(i)(c).

¹⁵⁹ See T.D. 7454, 1977-1 C.B. 367 (Preamble); see also Treas. Reg. § 1.6033-2(g)(5)(ii) (1977) (“An organization’s principal activity will not be considered to be exclusively religious if that activity is educational, literary, charitable, or of another nature (other than religious) that would serve as a basis for exemption under section 501(c)(3).”).

¹⁶⁰ Treas. Reg. § 1.6033-2(g)(5)(iv), example (2) (1977).

¹⁶¹ See I.R.C. § 6033(a)(2)(B) (1977); Treas. Reg. § 1.6033-2(g)(1)(vii) (1977); see also 42 Fed. Reg. 768 (Preamble). Whelan notes that the Secretary of the Treasury likely exercised his discretionary power to try to “deflect a very powerful argument against the validity of the new regulations with respect to parochial schools” because of recent Supreme Court decisions characterizing such schools as “substantially religious and closely identified” with the churches’ mission. Whelan, *supra* note 110, at 898 n.63. Whelan further comments that “[g]iven these decisions, it is unlikely that federal courts would agree with Treasury that these schools are not component ‘parts’ of the churches that operate them, even when they are separately incorporated.” *Id.* (citing *Levitt v. Comm. for Pub. Educ. & Religious Liberty*, 413 U.S. 472 (1973); *Lemon v. Kurtzman*, 403 U.S. 602 (1971)).

¹⁶² Hoff, *supra* note 128, at 92; see also *Lutheran Soc. Serv. of Minn. v. United States*, 583 F. Supp. 1298 (D. Minn. 1984), *rev’d*, 758 F.2d 1283, 1288–91 (8th Cir. 1985) (invalidating the portion of the regulation requiring an organization’s “principal activity” to be “exclusively religious” in order to qualify as an integrated auxiliary as an impermissible interpretation of § 6033); *Tenn. Baptist Children’s Homes, Inc. v. United States*, 604 F. Supp. 210, 213 (M.D. Tenn. 1984), *aff’d*, 790 F.2d 534 (6th Cir. 1986) (upholding the validity of the regulations, but only upon concluding that the organization was “exclusively religious,” thereby qualifying as an integrated auxiliary).

¹⁶³ Tax Reform Act of 1984, Pub. L. No. 98-369, § 2603, 98 Stat. 494, 1128 (1994) (codified at I.R.C. § 3121(w)(3)(B) (2000)); see also Hoff, *supra* note 128, at 92.

¹⁶⁴ Rev. Proc. 86-23, 1986-1 C.B. 564.

"admissions, goods, services, or facilities for sale, other than on an incidental basis, to the general public";¹⁶⁵ or (ii) offers admissions, goods or services for sale, other than on an incidental basis, to the general public and does not normally receive more than fifty percent of its support from a "combination of governmental sources; public solicitation of contributions," and receipts other than those from an unrelated trade or business.¹⁶⁶ If organizations receive a majority of their support from public and government sources rather than from church sources, the IRS reasoned that congressional intent would compel such organizations to file annual returns, thus providing opportunity for public inspection.¹⁶⁷ The other notion underlying this support test is that the organization's "religious activity" is attenuated if a majority of its support does not come from religious sources, thereby transforming the organization into a "*secular counterpart*."¹⁶⁸ This financial standard was subsequently imported into the final regulations under § 6033 addressing integrated auxiliaries.¹⁶⁹

3. Current Treatment of Integrated Auxiliaries

In late 1995, the IRS issued final regulations under § 6033 defining an "integrated auxiliary."¹⁷⁰ These regulations incorporate the internal support test of Revenue Procedure 86-23¹⁷¹ and further require that the organization be a separate entity that is (1) a "charitable" organization described in § 501(c)(3) (for example, a school, mission society, or youth group); (2) a public charity (as opposed to a private foundation);¹⁷²

¹⁶⁵ There's an exception for when the goods, services, or facilities are sold for a nominal charge or for substantially less than cost. *Id.*

¹⁶⁶ *Id.*

¹⁶⁷ T.D. 8640, 1996-1 C.B. 289, 290.

¹⁶⁸ George J. Blaine, *The Unfortunate Church-State Dispute Over the I.R.C. Section 6033 "Exclusively Religious" Activity Test*, 23 NEW ENG. L. REV. 1, 41 (1988) ("Too much outside secular support weakens the controlling church's influence on the organization, makes the organization responsive to secular forces, and presumably dilutes its religious content. In other words, the lack of sufficient in-house church support renders the organization a *secular counterpart*."); see also Hoff, *supra* note 128, at 92.

¹⁶⁹ See *infra* note 171 and accompanying text.

¹⁷⁰ T.D. 8640, 1996-1 C.B. 289.

¹⁷¹ Under current regulations, an organization is "internally supported" unless it both:

(i) Offers admissions, goods, services or facilities for sale, other than on an incidental basis, to the general public (except goods, services, or facilities sold at a nominal charge or for an insubstantial portion of the cost); and; (ii) Normally receives more than 50 percent of its support from a combination of governmental sources, public solicitation of contributions, and receipts from the sale of admissions, goods, performance of services, or furnishing of facilities in activities that are not unrelated trades or businesses.

Treas. Reg. § 1.6033-2(h)(4) (as amended in 1995).

¹⁷² See *supra* note 148.

and (3) “[a]ffiliated with a church or a convention or association of churches.”¹⁷³ An organization meets the “affiliated” requirement if it is covered by a group exemption letter issued to a church;¹⁷⁴ is operated, supervised, or controlled by that church; or if pertinent facts and circumstances establish such an affiliation.¹⁷⁵ The regulations provide a nonexclusive list of factors to determine affiliation, including that (i) the organization’s charter or bylaws reveal that it shares common religious doctrines or practices with a church or convention of churches, (ii) such church has the power to appoint, control, or remove at least one of the organization’s officers or directors, (iii) the organization’s name indicates an institutional relationship, (iv) the organization submits financial and operational reports at least annually to the church, (v) the church affirms its relationship with the organization, and (vi) upon dissolution, the organization’s assets are to be distributed to the church.¹⁷⁶

As set forth in the 1977 regulations, current regulations similarly provide that men’s and women’s organizations, seminaries, mission societies, and youth groups need not meet the internal support test to qualify as integrated auxiliaries, provided that all of the other components are satisfied.¹⁷⁷ Similarly, elementary and secondary schools need not satisfy the integrated auxiliary rules to be exempt from filing annual returns provided they are considered “affiliated” with a church under those rules or are operated by a religious order.¹⁷⁸ Accordingly, the clear import from the various interpretative regulations as well as the legislative history of the different acts affecting and changing § 6033 is simplistic yet pertinent: an organization must have some sort of “substantial connection” with a particular church as a condition of being considered an “integrated” auxiliary.¹⁷⁹

II. PROPOSALS TO COMBAT DISCRIMINATION BY RELIGIOUS ORGANIZATIONS

A. Overview of Alternative Proposals

As previously explained, the only potential restraint on discrimination by religious organizations exists in the public-policy doctrine enunciated by the United States

¹⁷³ Treas. Reg. § 1.6033-2(h)(1)(ii) (as amended in 1995).

¹⁷⁴ A group-exemption letter—or “group ruling”—requires the church’s central organization to report the entities and affiliates covered by its exemption annually to the IRS and to certify that each meets the requirements for exemption under § 501(c)(3). See CAFARDI & CHERRY, *supra* note 116, § 8.05.

¹⁷⁵ Treas. Reg. § 1.6033-2(h)(2) (as amended in 1995).

¹⁷⁶ *Id.* § 1.6033-2(h)(3); see also HOPKINS, *supra* note 48, § 10.5.

¹⁷⁷ Treas. Reg. § 1.6033-2(h)(5) (1977).

¹⁷⁸ Treas. Reg. § 1.6033-2(g)(1)(vii) (as amended in 1995). Neither the Code nor the regulations define “religious order.” Rather, under Revenue Procedure 91-20, an organization qualifies as a religious order based on certain attributes extracted from prior case law. Rev. Proc. 91-20, 1991-1 C.B. 524-25; see also HOPKINS, *supra* note 48, § 10.6.

¹⁷⁹ Whelan, *supra* note 110, at 915 n.125.

Supreme Court in *Bob Jones University v. United States*.¹⁸⁰ However, to date, only organizations that participated in racial discrimination, advocated civil disobedience, or were involved in an illegal activity have lost their tax-exempt status pursuant to the public-policy doctrine.¹⁸¹ Despite its clear importance in combating racial discrimination in education, the doctrine's main failure is its lack of a clearly-defined source of "established public policy."¹⁸² Namely, which sources of law or current policy should the IRS consult to determine that an established national policy exists?¹⁸³ Furthermore, of particular relevance, does discrimination on the basis of sexual orientation or marital status, as evidenced by examples herein, violate an established public policy? Legal scholars differ in their conclusions.¹⁸⁴ Critics also routinely comment that the public policy doctrine places too much discretion in a regulatory agency,¹⁸⁵ resulting in an evidentiary burden borne by the IRS to determine and prove that an organization's activities or policies violate a fundamental public policy.¹⁸⁶ Finally, some doubt exists as to the doctrine's applicability to churches or "other purely religious institutions," to which the Supreme Court alluded in its decision.¹⁸⁷

As addressed in my prior article, Professor David Brennen proposes expanding the applicability of civil rights laws to combat discrimination by charitable organizations, including religious organizations.¹⁸⁸ Although this expansion approach possesses significant potential, it nevertheless fails to address the kinds of discrimination illustrated in this Article.¹⁸⁹ Current civil rights laws have limited application in that they only protect against discrimination based on race, color, national or ethnic origin, religion, sex, age, and disability.¹⁹⁰ These laws do not prohibit discrimination on the bases of sexual orientation or marital status¹⁹¹—both of which appear to be common forms of discrimination currently engaged in by religious organizations.¹⁹² Although

¹⁸⁰ 461 U.S. 574, 586 (1983) (finding "unmistakable evidence" that the intent of § 501(c)(3) requires the institution to serve a "public purpose and not be contrary to established public policy").

¹⁸¹ Brennen, *Racial Discrimination*, *supra* note 45, at 391.

¹⁸² Mirkay, *Charities & Discrimination*, *supra* note 5, at 51, 67; *see also* Brennen, *Racial Discrimination*, *supra* note 45, at 403–04, 407, 436–39.

¹⁸³ Mirkay, *Charities and Discrimination*, *supra* note 5, at 67.

¹⁸⁴ *See supra* note 48 and accompanying text; *see also* Martha Minow, *Should Religious Groups Be Exempt from Civil Rights Laws?*, 48 B.C. L. REV. 781, 821 (2007) ("Neither national consensus nor federal power squarely guards against sexual orientation discrimination.").

¹⁸⁵ *See supra* note 49 and accompanying text.

¹⁸⁶ Mirkay, *Charities & Discrimination*, *supra* note 5, at 67; *see also* Hatfield, *supra* note 48, at 16.

¹⁸⁷ *See infra* notes 289–90 and accompanying text.

¹⁸⁸ *See* Brennen, *Tax Expenditures*, *supra* note 41, at 169.

¹⁸⁹ *See supra* notes 24–43 and accompanying text.

¹⁹⁰ *See* Brennen, *Tax Expenditures*, *supra* note 41, at 171–82; *see also* Minow, *supra* note 184.

¹⁹¹ Mirkay, *Charities & Discrimination*, *supra* note 5, at 82 nn.220–21.

¹⁹² *See supra* notes 24–43 and accompanying text; *see also* Mirkay, *Charities &*

Brennen acknowledged that discrimination on the basis of sexual orientation is “harmful discriminatory behavior,”¹⁹³ his expansion proposal fails to address such behavior adequately. The application of civil rights laws to address discrimination is further muddled by the fact that religious organizations are entitled to discriminate on the basis of religion in their employment decisions without violating Title VII of the Civil Rights Act of 1964.¹⁹⁴ Courts have routinely aligned with religious organizations on claims of sexual orientation discrimination in employment.¹⁹⁵ Accordingly, Congress would need to amend current civil rights laws to expressly prohibit discrimination on the basis of sexual orientation and marital status to truly abolish the discriminatory activities and policies exhibited herein. The congressional intent necessary to prohibit these kinds of discrimination by all private actors, including charitable and religious organizations, is dubious at best. Therefore, a more tailored legislative response targeting charitable and religious organizations may prove to be more effective.

B. Proposal—Narrowing Eligibility for Integrated Auxiliary Status to More Broadly Apply a Statutory Nondiscrimination Requirement

As previously mentioned, imposing a broad-based nondiscrimination requirement on religious organizations is difficult because of the constitutional concern of drawing too narrow a definition of “religious” or “church.”¹⁹⁶ As proposed in my prior article, churches should likely be exempt from a statutory nondiscrimination requirement due to constitutional concerns, primarily those originating from the First Amendment’s religion clauses.¹⁹⁷ While there is some constitutionally based analysis ostensibly supporting the imposition of a nondiscrimination requirement on churches,¹⁹⁸ there are other Free Exercise and Establishment Clause concerns, the answers to which are

Discrimination, *supra* note 5, at 48–50. Unless reported in the press or discussed in a court decision, the type and frequency of alleged or actual discrimination by religious organizations cannot be verified.

¹⁹³ Brennen, *Tax Expenditures*, *supra* note 41, at 169.

¹⁹⁴ 42 U.S.C. § 2000e-1(a) (2000) (“This subchapter shall not apply to an employer with respect to the employment of aliens outside any State, or to a religious corporation, association, educational institution, or society with respect to the employment of individuals of a particular religion to perform work connected with the carrying on by such corporation, association, educational institution, or society of its activities.”).

¹⁹⁵ Minow, *supra* note 184, at 808–10. Professor Minow astutely noted that “[a]lthough claims of discrimination on the basis of sexual orientation have not generated victories for plaintiffs suing religious organizations, neither have they done much to clarify the law.” *Id.* at 808.

¹⁹⁶ See *supra* text accompanying notes 59–63.

¹⁹⁷ The First Amendment provides, in part, that “Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof.” U.S. CONST. amend. I; see also *Lemon v. Kurtzman*, 403 U.S. 602 (1971).

¹⁹⁸ See *infra* notes 368–72 and accompanying text.

not clear.¹⁹⁹ These concerns arise from churches' purely religious mission and purpose, which is not necessarily present in the broader context of religious organizations whose purpose and mission may also encompass education, health, or social services. In applying the public policy doctrine, which is akin to a nondiscrimination requirement, the Supreme Court alluded to this distinction and a possible disparate outcome if the discriminating organization had been a church, stating that: "We deal here only with religious schools—not with churches or other purely religious institutions."²⁰⁰ Accordingly, this Article continues the proposal set forth in my prior article to exempt churches from the requirement, but more narrowly define the term "church." This narrow definition "should reflect the [IRS] fifteen-point test, with specific emphasis on the criterion of an established and dynamic congregation."²⁰¹ A church would only be exempt to the extent that the imposition of the discrimination requirement would be inconsistent with its established tenets or creed.²⁰² However, as previously stated, a church's professed tenets or creed cannot be questioned and must be accepted as genuine, absent a clear showing otherwise, to allay any potential claims under the First Amendment's religion clauses.²⁰³

The intent of the proposed nondiscrimination requirement is not to control or regulate the sincerely held religious beliefs of church members or those with whom they share their beliefs.²⁰⁴ Rather, it is to eliminate the use of tax-deductible dollars, and other benefits received by charitable and religious organizations pursuant to § 501(c)(3), to support or maintain discrimination against members of society.²⁰⁵ Accordingly, with respect to religious organizations, the most viable means of effecting this nondiscrimination proposal is to more narrowly define the statutory term "integrated auxiliary," thereby limiting the religious organizations functionally treated as churches under the Code.²⁰⁶

¹⁹⁹ See *infra* Part III.B.

²⁰⁰ *Bob Jones Univ. v. United States*, 461 U.S. 574, 604 n.29 (1983) (emphasis omitted).

²⁰¹ See Mirkay, *Charities & Discrimination*, *supra* note 5, at 100. To implement such an exemption, the article provided that § 501(c)(3) could be amended to include the following subparagraph: "In the case of a church, as defined in section 508(c)(1)(A), this shall not apply to the extent that the application would not be consistent with the church's established tenets or creed." *Id.* at 100 n.325.

²⁰² *Id.*

²⁰³ See *supra* notes 93–94 and accompanying text.

²⁰⁴ Mirkay, *Charities & Discrimination*, *supra* note 5, at 100.

²⁰⁵ *Id.* at 52–53.

²⁰⁶ Admittedly, this course of action does not address those activities that a church operates within its own legal entity; in other words, those activities not conducted in an entity separate from the church. Presumably, churches will still desire to operate activities in separate legal entities due to liability concerns, in which case a narrow definition of a church and, specifically, an integrated auxiliary, will subject at least some of those activities and entities to a nondiscrimination restriction. But see Rev. Rul. 75-231, 1975-1 C.B. 158, where the IRS determined that the public policy doctrine could be used to deny or revoke the exempt status of a church that

In attempting to draw a narrow definition of a church and its integrated auxiliaries, both the invalidated “principal activity” test of the 1977 regulations and its replacement, the internal support test, offer some valuable insights.²⁰⁷ In *Lutheran Social Service of Minnesota v. United States*, the Eighth Circuit determined that the “exclusively religious” component of the principal activity test in the 1977 regulations was contrary to congressional intent and “inconsistent with the legislative history of section 6033.”²⁰⁸ In addition to a statutory construction argument, the court reasoned that church-affiliated youth groups and men’s and women’s clubs—examples of integrated auxiliaries provided in the Senate and Conference Committee Reports from the 1969 Act—were “no more ‘exclusively religious’” than the plaintiff, a church-affiliated social service agency.²⁰⁹ However, those committee reports also listed mission societies and religious schools as examples of integrated auxiliaries, both of which can arguably be interpreted as predominantly religious in nature and less secular than a social service agency.²¹⁰ Therefore, the interpretation of what constitutes religious activity can be very subjective.

In substituting a less subjective internal support test for the exclusively religious principal activity test, the IRS borrowed from the financial support standard set forth in § 3121(w), “which permits certain church-related exempt organizations to elect out of social security coverage.”²¹¹ Section 3121(w) disallows an election for any church-controlled organizations that offer goods, services, or facilities for sale to the general public and receive greater than twenty-five percent of their support from such sales or governmental sources, or both.²¹² The legislative history provides that:

[M]any church-controlled organizations (including church-controlled universities and religious hospitals) provide services to the general public which are similar in nature to those provided by other, secular institutions. Allowing an election in these cases would result in differing treatment for employees of religious and secular organizations performing essentially similar functions Further, where an organization sells its services to the general

operated a racially discriminatory school within its own corporate entity because the school was not separately incorporated. In enacting Revenue Rule 75-231, the IRS relied on *Reynolds v. United States*, 98 U.S. 145, 166–67 (1878), and subsequent Supreme Court cases that concluded that, although the Free Exercise Clause bars government interference into religious beliefs, it does not necessarily “affect the legal consequences otherwise attending a given practice or action that is not inherently religious.” Rev. Rul. 75-231, 1975-1 C.B. 158.

²⁰⁷ See *supra* note 162.

²⁰⁸ 758 F.2d 1283, 1290–91 (8th Cir. 1985).

²⁰⁹ *Id.* at 1291.

²¹⁰ See *supra* note 140 and accompanying text.

²¹¹ T.D. 8640, 1996-1 C.B. 289.

²¹² I.R.C. § 3121(w)(3)(B) (2000).

public, concerns regarding the separation of church and state become less pressing.²¹³

To address these concerns, § 3121(w)(3) narrowly defines the eligibility of church-controlled organizations for the exemption election based on their activities and funding sources.²¹⁴ Congress concluded that these § 3121(w) rules “provide a fair, objective test for determining those organizations entitled to make an election without questioning the religious connection of any particular organization.”²¹⁵

The primary issue raised with respect to the internal support test adopted in both Revenue Procedure 86-23 and the current regulations under § 6033 is the reason the IRS used a fifty percent maximum threshold for permissible non-church funding rather than the twenty-five percent threshold used in § 3121(w)(3). Neither the revenue procedure nor the explanations under the notice of proposed rulemaking and final regulations offer any significant insights other than stating that the financial support requirement in the revenue procedure “is similar to, but more favorable than, the financial support requirement in section 3121(w).”²¹⁶ If integrated auxiliaries are truly intended to have a substantial connection with a church or convention of churches, one possible solution to ensuring that more church-affiliated entities are subject to the nondiscrimination requirement is to lower the maximum threshold of non-church funding. For example, the regulations could be amended to permit only those organizations whose funding from non-church sources does not exceed ten or twenty percent of their total support to be eligible for integrated auxiliary treatment.²¹⁷ At a minimum, a twenty-percent threshold would inversely comport with the required percentage ownership of related for-profit corporations desiring to file a single, consolidated return.²¹⁸ To avoid any confusion regarding applicability, such a restriction should be codified in § 508 or § 6033, as was done with § 3121(w), rather than governed solely by regulations.

If Congress’s intent in § 3121(w) was only to grant exemption to organizations with closely controlled church affiliations, such reasoning should equally apply in the context of limiting the grant of church tax exemption benefits, including an exemption from a statutory nondiscrimination requirement. Furthermore, as with the § 3121(w) test, reducing the amount of non-church funding for integrated auxiliary status attempts to “provide a fair, objective test . . . without questioning the religious connection of

²¹³ STAFF OF JOINT COMM. ON TAXATION, 98TH CONG., GENERAL EXPLANATION OF THE REVENUE PROVISIONS OF THE DEFICIT REDUCTION ACT 1214 (Comm. Print 1984).

²¹⁴ *Id.*

²¹⁵ *Id.*

²¹⁶ Prop. Treas. Reg. § 1.6033-2, 59 Fed. Reg. 64,633 (Dec. 15, 1994).

²¹⁷ See Whelan, *supra* note 110, at 924 n.159 (suggesting that organizations seeking to be integrated auxiliaries should not derive more than fifteen percent of their current operating budget from state or federal sources).

²¹⁸ See I.R.C. § 1504(a)(2) (2000).

any particular organization.”²¹⁹ Finally, in addition to more effectively addressing discrimination concerns, a lower non-church-funding threshold would further accomplish the congressional goal of providing increased opportunity for public inspection, and therefore greater transparency, of even more tax-exempt organizations.²²⁰

III. THE CONSTITUTIONALITY OF IMPOSING A SECTION 501(C)(3) NONDISCRIMINATION REQUIREMENT ON RELIGIOUS ORGANIZATIONS

A. First Amendment, Generally²²¹

The imposition of a nondiscrimination requirement on § 501(c)(3) organizations raises potential constitutional issues, primarily under the First Amendment.²²² Particular to religious organizations, the First Amendment’s two religion clauses—the Free Exercise Clause and the Establishment Clause—come into consideration, as discussed below.²²³ Nevertheless, one of the major criticisms of a nondiscrimination requirement is that it would violate an organization’s First Amendment free speech and association rights, because it “would significantly affect . . . [an organization’s] ability to advocate public or private viewpoints.”²²⁴ While the Supreme Court has not directly addressed this issue,²²⁵ it has upheld other restrictions on exempt organizations’ activities as conditions to exemption under § 501(c)(3), and has dismissed claims that such

²¹⁹ STAFF OF JOINT COMM. ON TAXATION, 98TH CONG., GENERAL EXPLANATION OF THE REVENUE PROVISIONS OF THE DEFICIT REDUCTION ACT 1214 (Comm. Print 1984).

²²⁰ See *supra* note 167 and accompanying text.

²²¹ Portions of the discussion in this subpart are substantially similar to a corresponding discussion contained in Mirkay, *Charities & Discrimination*, *supra* note 5, at 88–94.

²²² The First Amendment provides, “Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people peaceably to assemble, and to petition the Government for a redress of grievances.” U.S. CONST. amend. I. The amendment applies to state governments by operation of the Fourteenth Amendment. See *Everson v. Bd. of Educ.*, 330 U.S. 1 (1947).

²²³ See *infra* Part III.B.

²²⁴ *Boy Scouts of Am. v. Dale*, 530 U.S. 640, 650 (2000); see, e.g., Erez Reuveni, *On Boy Scouts and Anti-Discrimination Law: The Associational Rights of Quasi-Religious Organizations*, 86 B.U. L. REV. 109, 113 (2006) (contending that “quasi-religious” organizations like the Boy Scouts deserve “greater associational protections” under the First Amendment than purely secular organizations); Roy Whitehead, Jr. & Walter Block, *The Boy Scouts, Freedom of Association, and the Right to Discriminate: A Legal, Philosophical, and Economic Analysis*, 29 OKLA. CITY U. L. REV. 851, 882 (2004) (“Freedom of association is a necessary condition of a civilized order; laws prohibiting discrimination violate this freedom and must be repealed.”).

²²⁵ David A. Brennen, *Charities and the Constitution: Evaluating the Role of Constitutional Principles in Determining the Scope of Tax Law’s Public Policy Limitation for Charities*, 5 FLA. TAX REV. 779, 843 (2002); see also Mirkay, *Charities & Discrimination*, *supra* note 5, at 88–89.

restrictions constitute First Amendment violations.²²⁶ In discussing the interaction of constitutional rights and the income tax exemption, it is important to note that tax exemption is typically regarded as a congressional grant, not a constitutional right.²²⁷

One fundamental issue under First Amendment free speech analysis is whether the government can compel an organization to surrender its constitutional rights as a condition to receiving a public benefit, such as a tax exemption.²²⁸ In *Christian Echoes National Ministries v. United States*, a religious organization challenged the revocation of its tax exemption due to its substantial lobbying and political campaign activities in violation of § 501(c)(3).²²⁹ The Tenth Circuit disagreed with the Ministries' assertion that the lobbying and political campaign restrictions in § 501(c)(3) constituted unconstitutional conditions on its free speech rights:

In light of the fact that tax exemption is a privilege, a matter of grace rather than right, we hold that the limitations contained in Section 501(c)(3) withholding exemption from nonprofit corporations do not deprive Christian Echoes of its constitutionally guaranteed right of free speech. The taxpayer may engage in all such activities without restraint, subject, however, to withholding of the exemption or, in the alternative, the taxpayer may refrain from such activities and obtain the privilege of exemption.²³⁰

Similar reasoning was employed by the Supreme Court in *Regan v. Taxation With Representation of Washington*.²³¹ Taxation With Representation of Washington (TWR), a nonprofit organization, applied for, and was denied, § 501(c)(3) tax-exempt status due to its substantial lobbying activities.²³² In addressing TWR's argument that the lobbying limitation violated its First Amendment rights,²³³ the Court first characterized tax exemptions and the charitable contributions deduction as subsidies, analogizing such benefits to cash grants to the organization.²³⁴ The Court further clarified

²²⁶ See Brennen, *supra* note 225, at 843–44; *infra* notes 230–58 and accompanying text.

²²⁷ See *Comm'r v. Sullivan*, 356 U.S. 27, 28 (1958); *Christian Echoes Nat'l Ministry, Inc. v. United States*, 470 F.2d 849, 857 (10th Cir. 1972), *cert. denied*, 414 U.S. 864 (1973).

²²⁸ Oliver S. Thomas, *The Power to Destroy: The Eroding Constitutional Arguments for Church Tax Exemption and the Practical Effect on Churches*, 22 CUMB. L. REV. 605, 618 (1992); see *Speiser v. Randall*, 357 U.S. 513, 515–18 (1958) (holding that the State of California could not compel veterans to sign a loyalty oath as a condition to qualifying for a special property tax exemption for veterans).

²²⁹ 470 F.2d 852–53.

²³⁰ *Id.* at 857.

²³¹ 461 U.S. 540 (1983).

²³² *Id.* at 542.

²³³ *Id.*

²³⁴ *Id.* at 544. For additional references on equating tax exemption and the charitable contributions deduction with government subsidies, see sources cited *supra* note 41.

that Congress decided to more extensively subsidize nonprofit organizations' public welfare programs rather than their lobbying activities.²³⁵ Although it agreed with TWR's assertion that "the government may not deny a benefit to a person because he exercises a constitutional right,"²³⁶ the Court explained that the Code did not restrict TWR's ability to receive deductible contributions in support of its non-lobbying activities; Congress simply declined to finance lobbying activities with public funds.²³⁷ The Court further rejected the "notion that First Amendment rights are somehow not fully realized unless they are subsidized by the State."²³⁸

Significantly, the *Regan* Court reminded TWR that it still qualified for a tax exemption under § 501(c)(4) as a social-welfare organization, and that it could obtain deductible contributions for its nonlobbying activities by returning to the dual structure from which it originated²³⁹: two nonprofit corporations, one of which was tax-exempt under § 501(c)(3) and the other of which was tax-exempt under § 501(c)(4).²⁴⁰ The Court did, however, caution that the § 501(c)(3) organization should not subsidize the § 501(c)(4) entity, "otherwise, public funds might be spent on an activity Congress chose not to subsidize."²⁴¹

In his concurrence, Justice Harry Blackmun noted that "§ 501(c)(3) organizations retain their constitutional right to speak and to petition the Government" and agreed with the majority that a § 501(c)(3) organization can preserve both its tax exemption and its free speech rights by utilizing an affiliated § 501(c)(4) organization to carry out its lobbying pursuits.²⁴² Nevertheless, Justice Blackmun still cautioned that

[s]hould the IRS attempt to limit the control these organizations exercise over the lobbying of their § 501(c)(4) affiliates, the First Amendment problems would be insurmountable. It hardly answers one person's objection to a restriction on his speech that another person, outside his control, may speak for him. Similarly,

²³⁵ *Regan*, 461 U.S. at 544.

²³⁶ *Id.* at 545.

²³⁷ *Id.* at 545–46 (citing *Cammarano v. United States*, 358 U.S. 498 (1959) (involving a treasury regulation that forbade business deductions for lobbying expenses)).

²³⁸ *Id.* at 546 (citing *Cammarano*, 358 U.S. at 515 (Douglas, J., concurring)).

²³⁹ *Id.* at 544.

²⁴⁰ *Id.* The two nonprofit corporations merged to form Taxation With Representation of Washington. *Id.* at 543; *cf.* *FCC v. League of Women Voters*, 468 U.S. 364, 399–400 (1984) (finding that because a noncommercial educational broadcasting station was unable to practically separate its political and exempt activities into distinct § 501(c)(3) and § 501(c)(4) organizations, the federal law conditioning funding on the station's forbearance of its right to editorialize was an unconstitutional penalty).

²⁴¹ *Regan*, 461 U.S. at 544. To do so, the two entities should be "separately incorporated and keep records adequate to show that tax-deductible contributions are not used to pay for lobbying." *Id.* at 545 n.6.

²⁴² *Id.* at 553 (Blackmun, J., concurring).

an attempt to prevent § 501(c)(4) organizations from lobbying explicitly on behalf of their § 501(c)(3) affiliates would perpetuate § 501(c)(3) organizations' inability to make known their views on legislation without incurring the unconstitutional penalty. Such restrictions would extend far beyond Congress' mere refusal to subsidize lobbying.²⁴³

In other words, § 501(c)(4) arguably provides a constitutional safety hatch when imposing restrictions on the activities and possible constitutional rights of charitable organizations.

After *Regan*, churches attempted to distinguish the decision on the basis that applying the statutory restrictions on lobbying and political campaign activities to religious organizations implicated additional constitutional issues.²⁴⁴ However, as evidenced in the D.C. Circuit's decision in *Branch Ministries v. Rossotti*,²⁴⁵ religious organizations "appear to be on an equal footing with their secular counterparts" with respect to free speech challenges to the activity restrictions within § 501(c)(3).²⁴⁶

In *Branch Ministries*, a tax-exempt church, conducting business as the Church at Pierce Creek (CPC), placed a full-page advertisement in two newspapers four days before the 1992 presidential election.²⁴⁷ The advertisements urged Christians to vote against the Democratic candidate Bill Clinton because of his "positions on certain moral issues."²⁴⁸ Each advertisement attributed co-sponsorship to CPC and solicited tax-deductible donations in support of its cause.²⁴⁹ In response, the IRS invoked a statutorily prescribed church-tax inquiry,²⁵⁰ followed by a church-tax examination.²⁵¹ Ultimately concluding that the placement of the advertisements violated the statutory prohibition on political campaign activity, the IRS revoked CPC's § 501(c)(3) tax-exempt status.²⁵² CPC challenged the revocation, alleging that the revocation violated

²⁴³ *Id.*

²⁴⁴ Thomas, *supra* note 228, at 625.

²⁴⁵ 211 F.3d 137 (D.C. Cir. 2000).

²⁴⁶ Thomas, *supra* note 228, at 626.

²⁴⁷ *Branch Ministries*, 211 F.3d at 139.

²⁴⁸ *Id.* Each advertisement displayed the headline "Christians Beware" and declared that Clinton's stances on abortion, homosexuality, and the distribution of condoms to teenage students were contrary to "Biblical precepts." *Id.* at 140.

²⁴⁹ *Id.*

²⁵⁰ See *id.* Specific statutory rules govern the IRS's ability to audit churches. See I.R.C. § 7611 (2000). A "church tax inquiry" may only be initiated by an appropriate IRS official (typically, a regional commissioner or person of higher rank within the IRS) who "reasonably believes, on the basis of facts and circumstances recorded in writing, that the organization may not qualify for tax exemption as a church" because of certain nonexempt activities. HOPKINS, *supra* note 48, § 26.6(c); see also I.R.C. § 7611(a)(1)(A), (a)(2).

²⁵¹ See *Branch Ministries*, 211 F.3d at 140; see also I.R.C. § 7611(h)(3).

²⁵² *Branch Ministries*, 211 F.3d at 140.

its free exercise and free speech rights under the Religious Freedom Restoration Act of 1993 and the First Amendment.²⁵³

With respect to the free speech claim, the D.C. Circuit, relying on *Regan*, concluded that CPC had “an alternate means of communication” through the formation and operation of an affiliated organization exempt under § 501(c)(4).²⁵⁴ The court explained that, while they are subject to a similar ban on political campaign activities, § 501(c)(4) organizations may form a political action committee that can participate in political campaigns without limitation.²⁵⁵ Still, the court reminded CPC that it could not channel its tax-deductible contributions to fund the political action committee because Congress chose not to subsidize such First Amendment activities.²⁵⁶

As in Justice Blackmun’s concurrence in *Regan*, which deemed the availability of a § 501(c)(4) organization as an alternate means of communication to be “essential to the constitutionality of § 501(c)(3)’s restrictions on lobbying,”²⁵⁷ *Branch Ministries* relied on this availability to sustain the constitutionality of § 501(c)(3)’s prohibition on political campaign activities.²⁵⁸ Accordingly, it seems probable that these alternate means of communication might be of similar utility in sustaining the constitutionality of a nondiscrimination requirement in § 501(c)(3) with respect to religious organizations. As with the lobbying and political campaign restrictions, a religious organization would be free to discriminate in the activities conducted within a § 501(c)(4) affiliate without jeopardizing its tax benefits as to its nondiscriminatory activities.

Professor Eugene Volokh, a constitutional law scholar, comprehensively addressed whether the government may limit its “subsidies”—direct grants, tax exemptions and deductions, and access to government property—to organizations or groups that do not discriminate on a wide variety of bases.²⁵⁹ He acknowledged that discrimination on the basis of race, ethnicity, religion, sex, or sexual orientation may often be a constitutional right, as the Supreme Court concluded in *Boy Scouts of America v. Dale*.²⁶⁰

²⁵³ *Id.* at 140–41. See *infra* notes 306–10 and accompanying text for a discussion on CPC’s free exercise claim.

²⁵⁴ See *Branch Ministries*, 211 F.3d at 143 (citing *Regan v. Taxation With Representation of Wash.*, 461 U.S. 540, 552 (1983)).

²⁵⁵ *Id.* (citing Treas. Reg. § 1.527-6(f) to (g) (1980)). The court reminded CPC that the “related § 501(c)(4) organization must be separately incorporated; and it must maintain records that will demonstrate that tax-deductible contributions to the Church have not been used to support the political activities conducted by the § 501(c)(4) organization’s political action arm.” *Id.*

²⁵⁶ *Id.* at 143–44 (citing *Regan*, 461 U.S. at 548).

²⁵⁷ *Id.* at 143 (citing *Regan*, 461 U.S. at 552–53 (Blackmun, J., concurring)).

²⁵⁸ *Id.*

²⁵⁹ See Eugene Volokh, *Freedom of Expressive Association and Government Subsidies*, 58 STAN. L. REV. 1919, 1920 (2006). Professor Volokh preliminarily concludes that federal and state tax exemptions, including the charitable contributions deduction, are “tantamount to a matching grant.” *Id.* at 1920 n.1; see also *supra* note 41.

²⁶⁰ Volokh, *supra* note 259 (citing *Boy Scouts of Am. v. Dale*, 530 U.S. 640, 644 (2000) (holding that New Jersey’s public-accommodations law, which prohibited discrimination on

Nevertheless, he opined that the government may have a completely plausible reason for imposing a nondiscrimination condition on subsidy eligibility; namely, “the commonly held view that discrimination is generally wrong and thus generally should not be subsidized by the government.”²⁶¹

Similar to the reasoning espoused in *Christian Echoes* and *Regan*, Volokh centered his First Amendment analysis on his “No Duty to Subsidize Principle,” which provides that the government is not constitutionally required to fund the exercise of constitutionally-granted freedoms and rights.²⁶² However, his principle will govern, provided that it does not constitute governmental viewpoint or religious discrimination.²⁶³ In other words, the government may not differentiate among speakers based on their viewpoint or exclude religious conduct from governmental subsidies when it funds “equivalent secular conduct.”²⁶⁴

With respect to governmental viewpoint discrimination, Volokh provided the following example:

Excluding the Boy Scouts and all other discriminating groups from a government charitable fund drive is content-neutral and generally permissible. Excluding only the Scouts, but not other groups that equally violate the antidiscrimination policy, may show that the government is acting because of the viewpoint the Scouts express and not because of the discriminatory actions that the Scouts take.²⁶⁵

In the context of governmental religious discrimination, Volokh acknowledged that a nondiscrimination requirement could affect religious organizations more than secular ones, because “religious groups would derive more benefit from the ability to discriminate based on religious ideology.”²⁶⁶ However, he noted that laws that prohibit certain practices that are central to a religious group’s rituals yield the same result, as illustrated in the following example:

Peyote laws, for instance, have a more serious effect on religious groups that see peyote use as a sacrament than on most secular

the basis of sexual orientation, violated the Boy Scouts’ First Amendment rights—specifically, the freedom of expressive association—and upholding the organization’s right to exclude homosexuals from its membership)).

²⁶¹ *Id.* at 1934; see, e.g., Ian Urbina, *Boy Scouts Lose Philadelphia Lease in Gay-Rights Fight*, N.Y. TIMES, Dec. 6, 2007, at A26.

²⁶² Volokh, *supra* note 259, at 1922; see also *Regan v. Taxation With Representation of Wash.*, 461 U.S. 540, 547–49 (1983).

²⁶³ Volokh, *supra* note 259, at 1922.

²⁶⁴ *Id.*

²⁶⁵ *Id.* at 1931 (citations omitted).

²⁶⁶ *Id.* at 1937.

groups whose members may just want to experiment with peyote. Yet such a disparate impact, even when it substantially burdens a group's exercise of religion, does not even render unconstitutional *criminal prohibitions* of practices. It surely wouldn't bar *the exclusion from benefit programs* of groups that engage in those practices.²⁶⁷

Therefore, Volokh ultimately determined that the viewpoint and religious discrimination exceptions to his "No Duty to Subsidize Principle" do not effectively prevent the government from instituting nondiscrimination conditions on subsidies it provides, such as tax exemption.²⁶⁸

B. The First Amendment's Two Religion Clauses

The federal income tax exemption of religious organizations, including any restriction on that exemption, raises two additional fundamental constitutional issues,²⁶⁹ both of which arise under the First Amendment's two religion clauses—the Establishment Clause and the Free Exercise Clause.²⁷⁰ The Establishment Clause essentially disallows "governmentally established religion,"²⁷¹ while the Free Exercise Clause forbids "governmental interference with religion."²⁷² Supreme Court jurisprudence reflects the distinct separateness of these two clauses, creating a tension discussed *ad infinitum* by legal scholars.²⁷³ Specifically, the Supreme Court has acknowledged its own dilemma in finding "a neutral course between the two Religion Clauses, both of which are cast in absolute terms, and either of which, if expanded to a logical extreme, would tend to clash with each other."²⁷⁴ The tension also exists within each clause itself. For example, while clearly stating that the Establishment Clause does

²⁶⁷ *Id.* (citations omitted).

²⁶⁸ *Id.* at 1922–23; see also Mary E. Becker, *The Politics of Women's Wrongs and the Bill of "Rights": A Bicentennial Perspective*, 59 U. CHI. L. REV. 453, 484–85 (1992) (proposing the loss of tax exemption for organizations that employ gender discrimination in choosing their leaders); cf. Richard W. Garnett, *A Quiet Faith? Taxes, Politics, and the Privatization of Religion*, 42 B.C. L. REV. 771, 796 (2001) (arguing that, by placing restrictions on religious organizations' exemption, "government subtly reshapes religious consciousness itself").

²⁶⁹ Gaffney, *Federal Taxation*, *supra* note 121, at 412.

²⁷⁰ U.S. CONST. amend. I.

²⁷¹ Kenneth C. Halcom, *Taxing God*, 38 MCGEORGE L. REV. 729, 745 (2007) (citing *Walz v. Tax Comm'n*, 397 U.S. 664, 669 (1970)).

²⁷² *Walz*, 397 U.S. at 669.

²⁷³ See, e.g., Edward McGlynn Gaffney, Jr., *Exemption of Religious Communities from State and Local Taxation*, in RELIGIOUS ORGANIZATIONS IN THE UNITED STATES, *supra* note 121, at 459, 470; Halcom, *supra* note 271 (citing MICHAEL W. MCCONNELL ET AL., RELIGION AND THE CONSTITUTION (2002)); Witte, *supra* note 50, at 364.

²⁷⁴ *Walz*, 397 U.S. at 668–69.

not prohibit tax exemption for religious organizations,²⁷⁵ the Supreme Court has also ruled that a tax exemption granted only to religious organizations does violate the clause.²⁷⁶ Similarly, in the context of the Free Exercise Clause, the Supreme Court has upheld the imposition of a generally applicable sales tax on religious organizations' materials, but the extent to which such imposition of tax would survive any free exercise challenges is subject to conjecture.²⁷⁷ Accordingly, the effect of these two religion clauses on restricting the income tax exemption of religious organizations pursuant to § 501(c)(3) requires further and more detailed exploration.

1. Free Exercise Clause

Free exercise cases typically involve a clash between a person's religious beliefs and a secular law.²⁷⁸ Traditional Free Exercise Clause analysis prohibits any government action that substantially burdens religious practices.²⁷⁹ Provided the claimant establishes that her conduct is compelled by a sincerely held religious belief and the government has burdened this conduct in some way, the burden of proof shifts to the government to prove that it has acted in the least burdensome way possible in furthering its compelling interest.²⁸⁰ The United States Supreme Court's decisions in *Murdock v. Pennsylvania (City of Jeannette)*²⁸¹ and *Follett v. Town of McCormick*²⁸² employed this traditional analysis.²⁸³ Both cases involved local municipal ordinances that imposed a flat license tax or fee on the sale of merchandise within the city or town. These license taxes were imposed on Jehovah's Witnesses distributing religious literature.²⁸⁴ In both cases, the Supreme Court

²⁷⁵ *Id.* at 664.

²⁷⁶ *Tex. Monthly, Inc. v. Bullock*, 489 U.S. 1, 14 (1989).

²⁷⁷ *Jimmy Swaggart Ministries v. Bd. of Equalization of Cal.*, 493 U.S. 378 (1990); *see also Halcom*, *supra* note 271, at 746.

²⁷⁸ *HOPKINS*, *supra* note 48, § 10.1(a)(i).

²⁷⁹ *Thomas*, *supra* note 228, at 609 (citing *Sherbert v. Verner*, 374 U.S. 398 (1963) (finding an unconstitutional denial of unemployment benefits due to a member of the Seventh-Day Adventist Church who resisted working on Saturdays in accordance with her religious beliefs); *Wisconsin v. Yoder*, 406 U.S. 205 (1972) (discussing the unconstitutionality of requiring Amish parents to send their grade school graduates to high school)).

²⁸⁰ *Sherbert*, 374 U.S. at 403–07.

²⁸¹ 319 U.S. 105 (1943).

²⁸² 321 U.S. 573 (1944).

²⁸³ *Murdock* and *Follett* are typically viewed as cases implicating the free exercise of religion, but as some legal scholars observe, "[T]he results [in both cases] are also harmonious with the requirements of the nonestablishment provision." Edward McGlynn Gaffney, Jr., *Exemption of Religious Communities from State and Local Taxation*, in *RELIGIOUS ORGANIZATIONS IN THE UNITED STATES*, *supra* note 121, at 476. The author later opines that "[n]either *Murdock* nor *Follett* yielded opinions grounded in both nonestablishment and free exercise concerns." *Id.* at 477.

²⁸⁴ *Follett*, 321 U.S. at 574; *Murdock*, 319 U.S. at 106.

found that the imposition of the tax violated the petitioners' First Amendment rights to freely exercise their religion.²⁸⁵ Although, as the dissents pointed out, the challenged license taxes were generally applicable to all persons and religiously neutral,²⁸⁶ these taxes were ultimately struck down because they constituted "prior restraint[s] on the free exercise of religious beliefs."²⁸⁷

Distinguishing *Murdock* and *Follett* in light of more recent Supreme Court cases, some legal scholars opine that the First Amendment's Free Exercise Clause does not absolutely require that religious organizations be exempt from taxation.²⁸⁸ In fact, the *Murdock* Court cautioned that its decision did not mean that "religious groups . . . are free from all financial burdens of government."²⁸⁹ Based on the Supreme Court's decision in *Employment Division v. Smith*,²⁹⁰ a broadly applicable and religion-neutral tax should not raise free exercise concerns nor compel a local or state government to grant an exemption to any individual or organization, provided it does not constitute a prior restraint on religious activity.²⁹¹ As the Supreme Court reasoned in *Smith*, "if prohibiting the exercise of religion (or burdening the activity of printing) is not the object of the tax but merely the incidental effect of a generally applicable and otherwise valid provision, the First Amendment has not been offended."²⁹² As explained by one legal scholar, "*Smith* understood the Free Exercise Clause to provide an 'equality' right—a requirement of special justification for the *discriminatory* burdening of religious exercise—rather than a 'substantive' right—a requirement of special justification for *any* burdening . . . of religious exercise."²⁹³ Accordingly, under *Smith*, the government cannot impose a nondiscrimination condition on § 501(c)(3) tax-exempt status only as to religious organizations, but it can impose and enforce such a condition as to all organizations seeking exemption thereunder.²⁹⁴

This distinction is best exemplified by the decision in *Jimmy Swaggart Ministries v. Board of Equalization*, in which the Supreme Court unanimously determined that

²⁸⁵ *Follett*, 321 U.S. at 573; *Murdock*, 319 U.S. at 112.

²⁸⁶ See *Murdock*, 319 U.S. at 118 (Reed, J., dissenting) ("No evidence is offered to show the amount is oppressive. . . . There is no contention in any of these cases that such discrimination is practiced in the application of the ordinances.").

²⁸⁷ *Halcom*, *supra* note 271, at 751.

²⁸⁸ *Id.* at 750 (citing JOHN E. NOWAK & RONALD D. ROTUNDA, CONSTITUTIONAL LAW § 17.8 (2000)). However, in *Walz*, Justice Burger asserted that tax exemption "operated affirmatively to help guarantee the free exercise of all forms of religious belief." *Walz v. Tax Comm'n*, 397 U.S. 664, 678 (1970).

²⁸⁹ *Murdock*, 319 U.S. at 112.

²⁹⁰ 494 U.S. 872 (1990).

²⁹¹ *Halcom*, *supra* note 271, at 750 (citing JOHN E. NOWAK & RONALD D. ROTUNDA, CONSTITUTIONAL LAW § 17.8 (2000)). See generally *Jimmy Swaggart Ministries v. Bd. of Equalization*, 493 U.S. 378 (1990).

²⁹² *Employment Div.*, 494 U.S. at 878.

²⁹³ Patrick J. Schiltz & Douglas Laycock, *Employment in Religious Organizations*, in RELIGIOUS ORGANIZATIONS IN THE UNITED STATES, *supra* note 121, at 527, 549.

²⁹⁴ *Id.* at 549–50.

a California sales and use tax that was broadly applied and religiously neutral did not offend the Free Exercise Clause.²⁹⁵ More importantly, the Court stated that the Free Exercise Clause “does not *require* the State to grant appellant an exemption” from a generally applicable tax.²⁹⁶ In so stating, the Court distinguished *Murdock* and *Follett* on the basis that the flat-tax or license fee at issue in those cases “operate[d] as a prior restraint on the free exercise of religious beliefs.”²⁹⁷ The Court cautioned, however, that “a more onerous tax rate, even if generally applicable,” could raise free exercise concerns.²⁹⁸ Although the Court did not speculate as to when a tax rate would be “onerous,”²⁹⁹ it did note earlier in its opinion that the California tax constituted only a “small fraction of any retail sale.”³⁰⁰

A free exercise claim was also raised in *Bob Jones University v. United States*.³⁰¹ In response to the university’s argument that the public-policy doctrine violated its First Amendment free exercise rights, the Supreme Court affirmed that certain compelling governmental interests can justify regulating certain religious conduct.³⁰² In finding that the government’s interest in eradicating racial discrimination in education was sufficiently compelling to overcome any First Amendment concerns, the Court concluded that the “[d]enial of tax benefits will inevitably have a substantial impact on the operation of private religious schools, but will not prevent those schools from observing their religious tenets.”³⁰³ The Court alluded to a disparate outcome if the claimant had been a church,³⁰⁴ stating that: “We deal here only with religious *schools*—not with churches or other purely religious institutions; here, the governmental interest is in denying public support to racial discrimination in education.”³⁰⁵

In *Branch Ministries*, CPC raised a free exercise claim with regard to the revocation of its tax-exempt status due to prohibited political campaign activity.³⁰⁶ In response to that claim, the D.C. Circuit found that CPC failed to establish that the

²⁹⁵ *Jimmy Swaggart Ministries*, 493 U.S. at 389–90.

²⁹⁶ *Id.* at 392.

²⁹⁷ *Id.* at 389.

²⁹⁸ *Id.* at 392.

²⁹⁹ *Id.*

³⁰⁰ *Id.* at 389; *see also* Halcom, *supra* note 271, at 751–52.

³⁰¹ 461 U.S. 574 (1983).

³⁰² *Id.* at 603. The Court relied, in part, on *Prince v. Massachusetts*, 321 U.S. 158 (1944), which held that “neutrally cast child labor laws prohibiting sale of printed materials on public streets could be applied to prohibit children from dispensing religious literature.” *Bob Jones Univ.*, 461 U.S. at 603.

³⁰³ *Bob Jones Univ.*, 461 U.S. at 603–04. The Court further concluded that the government’s interest “substantially outweighs whatever burden denial of tax benefits places on petitioners’ exercise of their religious beliefs. The interests asserted by [the university] cannot be accommodated with that compelling governmental interest, and no ‘less restrictive means’ are available to achieve the governmental interest.” *Id.* at 604 (citations omitted).

³⁰⁴ Thomas, *supra* note 228, at 614.

³⁰⁵ *Bob Jones Univ.*, 461 U.S. at 604 n.29.

³⁰⁶ *Branch Ministries v. Rossotti*, 211 F.3d 137, 140–41 (D.C. Cir. 2000).

revocation had substantially burdened its free exercise rights and the lack of a compelling governmental interest justifying such a burden.³⁰⁷ The court further concluded that CPC's loss of its exemption for violating the political campaign prohibition did not constitute an unconstitutional burden on its free exercise rights. This would only be true, explained the court, "if the receipt of the privilege (in this case the tax exemption) is conditioned 'upon conduct proscribed by a religious faith, or . . . denie[d] . . . because of conduct mandated by religious belief, thereby putting substantial pressure on an adherent to modify his behavior and to violate his beliefs.'"³⁰⁸ The court concluded that the revocation would only result in decreased funds to support CPC's religious practices. However, the Supreme Court had previously determined that this financial burden lacked constitutional significance.³⁰⁹ Furthermore, the court found that CPC's alleged burden was exaggerated because of the special treatment churches receive under the Code, thereby rendering the revocation's impact "more symbolic than substantial."³¹⁰

Accordingly, based on the above case law, provided a tax (I) does not constitute a prior restraint on religious activity, (ii) does not have as its primary purpose to impede such activity, (iii) is applied in a broad and religiously neutral manner, and (iv) does not impose too high of a rate, neither the taxation of, nor a restriction on an exemption granted to, religious organizations, should likely raise any free exercise concerns.

However, Professor Volokh raised a perplexing dilemma with respect to free exercise concerns implicated by a nondiscrimination condition on government subsidies—namely, the effect of the Religious Freedom Restoration Act (RFRA) and its state counterparts.³¹¹ As previously explained, the Supreme Court's 1990 decision in *Employment Division v. Smith* ostensibly ended any free exercise concerns with

³⁰⁷ See *id.* at 142 (citing *Jimmy Swaggart Ministries v. Bd. of Equalization*, 493 U.S. 378, 384–85 (1990) ("[T]he free exercise inquiry asks whether government has placed a substantial burden on the observation of a central religious belief or practice and, if so, whether a compelling governmental interest justifies the burden.")); see also 42 U.S.C. § 2000bb-1(a) to (b) (2000), *invalidated in part by City of Boerne v. Flores*, 521 U.S. 507 (1997) (providing that the government can only substantially burden a person's exercise of religion if that burden is "in furtherance of a compelling governmental interest" and "is the least restrictive means of furthering" that interest).

³⁰⁸ *Branch Ministries*, 211 F.3d at 142 (quoting *Jimmy Swaggart Ministries*, 493 U.S. at 391–92).

³⁰⁹ *Id.* (quoting *Jimmy Swaggart Ministries*, 493 U.S. at 391); see also *Hernandez v. Comm'r*, 490 U.S. 680, 700 (1989) ("[P]etitioners' claimed exemption stems from the contention that an incrementally larger tax burden interferes with their religious activities. This argument knows no limitation.").

³¹⁰ *Branch Ministries*, 211 F.3d at 142. The court further explained that, if CPC did not intervene in future political campaigns, it could "hold itself out as a 501(c)(3) organization and receive all the benefits of that status. All that will have been lost, in that event, is the advance assurance of deductibility in the event a donor should be audited." *Id.* at 142–43.

³¹¹ Religious Freedom Restoration Act of 1993, 42 U.S.C. § 2000bb-1 (2000), *invalidated in part by City of Boerne v. Flores*, 521 U.S. 507 (1997); see *supra* note 307.

respect to tax exemption.³¹² *Smith* held that “if prohibiting the exercise of religion . . . is not the object of the tax but merely the incidental effect of a generally applicable and otherwise valid provision, the First Amendment has not been offended.”³¹³ In response to the appeal of a broad coalition of religious organizations,³¹⁴ the federal government enacted the RFRA, which was modeled after pre-*Smith* case law that granted exemptions from generally applicable laws, including subsidies, to religious objectors pursuant to the Free Exercise Clause.³¹⁵ By providing a remedy to these religious objectors, the RFRA “shifted the burden of proof . . . back to the government.”³¹⁶ A number of states followed the RFRA either by enacting legislation or by interpreting their state constitutions to hold similarly that the “[g]overnment shall not substantially burden a person’s exercise of religion even if the burden results from a rule of general applicability,” unless it “is in furtherance of a compelling governmental interest and is the least restrictive means of furthering that compelling government interest.”³¹⁷ Accordingly, under the RFRA and its progeny, organizations with discriminatory policies or practices have a “constitutional right to religious accommodation” permitting them to disregard a subsidy’s nondiscrimination condition while continuing to receive the subsidy.³¹⁸

In addressing the effect of the RFRA, Volokh posed a significant issue: whether the government’s refusal to subsidize discrimination based on religious beliefs or tenets constitutes a “substantial burden” on free exercise.³¹⁹ For example, in *Bob Jones University*, decided prior to *Smith*, the Supreme Court found that although the revocation of tax exemption could have a “substantial impact” on private religious schools’ operation, it “will not prevent those schools from observing their religious tenets.”³²⁰ The Court further determined that the government’s interest in eliminating racial discrimination in education “substantially outweighs whatever burden denial of tax benefits” placed on the university’s free exercise rights.³²¹ Nevertheless, Volokh concluded that under these pre-*Smith* cases, and thus presently under the RFRA, an

³¹² See *supra* notes 290–94 and accompanying text.

³¹³ *Employment Div. v. Smith*, 494 U.S. 872, 878 (1990).

³¹⁴ Edward McGlynn Gaffney, Jr., *Full and Free Exercise of Religion*, in *RELIGIOUS ORGANIZATIONS IN THE UNITED STATES*, *supra* note 121, at 773, 803.

³¹⁵ Volokh, *supra* note 259, at 1949–50.

³¹⁶ Edward McGlynn Gaffney, Jr., *Full and Free Exercise of Religion*, in *RELIGIOUS ORGANIZATIONS IN THE UNITED STATES*, *supra* note 121, at 803.

³¹⁷ Volokh, *supra* note 259, at 1950 & n.117 (quoting 42 U.S.C. § 2000bb-1(a), (b)); see also Hatfield et al., *supra* note 48, at 73 (“Congress made clear in its declaration of findings and purposes that the purpose of the law was to force the courts to utilize the compelling interest test in all cases in which the free exercise of religion is substantially burdened.”).

³¹⁸ Volokh, *supra* note 259, at 1950.

³¹⁹ *Id.* at 1954. Volokh also addressed the issue of when the “exercise of religion” is implicated and by whom, thus triggering the statutory right to accommodation. See *id.* at 1951–54.

³²⁰ *Bob Jones Univ. v. United States*, 461 U.S. 574, 603–04 (1982).

³²¹ *Id.* at 604.

organization which engaged in discrimination as a religious practice would likely continue to receive subsidies if the government did not have a compelling interest to “trump the religious freedom right,” such as an interest in eradicating sexual orientation discrimination.³²² But, as to a compelling governmental interest, Volokh flipped that statement on its head and asked “whether the government has a compelling interest in *refusing to fund* the discrimination, even if it lacks a compelling interest in prohibiting the discrimination.”³²³ Although concluding that both pre-*Smith* free exercise case law and the RFRA and its state progeny provide little, if any, answers,³²⁴ he opined that an interest in not funding discrimination was likely not compelling.³²⁵ Although Volokh initially concluded that it was difficult to determine whether a discriminating organization would prevail under a RFRA-based claim, he nevertheless predicted that such an organization would likely not prevail if the issue of its right to receive government subsidies were before the Supreme Court.³²⁶

In conclusion, Volokh asserted that an organization’s loss of governmental subsidies as a result of its discriminatory practices would not be a “terribly dire” consequence.³²⁷ First, such organizations can frequently obtain subsidies through the politically driven legislative process.³²⁸ For example, if the proposed nondiscrimination requirement set forth in this Article were imposed on tax exemption under § 501(c)(3), the government would likely succumb to political pressure and exempt churches.³²⁹ Second, Volokh concluded practically that discriminating organizations that lose their eligibility for receiving deductible contributions “will be no worse off than lobbying or electioneering organizations, many of which thrive despite their lack of tax-exempt status.”³³⁰

2. Establishment Clause

Most people associate the First Amendment’s Establishment Clause with prohibiting the government from favoring one religion over another, not necessarily with justification for tax exemption.³³¹ Because religious organizations are regulated by the government as tax-exempt organizations, the Establishment Clause is necessarily

³²² Volokh, *supra* note 259, at 1956 (citing *Boy Scouts of Am. v. Dale*, 530 U.S. 640, 658–59 (2000)); *see also* *DeSantis v. Pac. Tel. & Tel. Co.*, 608 F.2d 327, 333 (9th Cir. 1979) (“The courts have not designated homosexuals a ‘suspect’ or ‘quasi-suspect’ classification so as to require more exacting scrutiny of classifications involving homosexuals.”).

³²³ Volokh, *supra* note 259, at 1963.

³²⁴ *Id.*

³²⁵ *Id.* at 1964.

³²⁶ *Id.* at 1951, 1968.

³²⁷ *Id.* at 1924.

³²⁸ *Id.* at 1924, 1967.

³²⁹ *Id.* at 1967.

³³⁰ *Id.* at 1924, 1967.

³³¹ *Halcom*, *supra* note 271, at 752; *Thomas*, *supra* note 228, at 627.

implicated,³³² specifically, the “no excessive government entanglement” prong of a three-part test utilized by the Supreme Court in addressing establishment issues.³³³

In *Lemon v. Kurtzman*, the Supreme Court determined that a state program that provided financial assistance to parochial schools for the teaching of secular subjects was unconstitutional under the Establishment Clause.³³⁴ In reaching its conclusion, the Court announced a three-prong test assembled from its previous Establishment Clause cases.³³⁵ Under *Lemon*, any state program or law (1) must have a secular purpose; (2) its principal or primary effect must neither advance nor inhibit religion; and (3) it must not promote or foster an “excessive government entanglement with religion.”³³⁶ If a tax (or an exemption from tax) is broadly applicable and religiously neutral, as in *Jimmy Swaggart Ministries*,³³⁷ then the first two prongs of the *Lemon* test are generally not implicated. It is typically the third prong’s prohibition on excessive entanglement between the government and religion that is likely implicated by any tax imposed on, or restriction on an exemption granted to, religious organizations.³³⁸ For example, in *Lemon*, the state’s ability to “inspect and evaluate” the parochial school’s financial records for purposes of ascertaining religious and secular expenditures created, according to the Court, “an intimate and continuing relationship between church and state.”³³⁹

In a decision handed down concurrently with *Lemon*, the Supreme Court identified several factors that could lead to excessive entanglement, namely, a continuing

³³² HOPKINS, *supra* note 48, § 10.1(a)(ii).

³³³ *Id.* (specifically articulating the entanglement as “sponsorship, financial support, and active involvement of the sovereign in religious activity” (quoting *Lemon v. Kurtzman*, 403 U.S. 602, 612 (1971))).

³³⁴ 403 U.S. 602, 608–09, 613–14 (1971).

³³⁵ *Id.* at 612.

³³⁶ *Id.* at 612–13 (quoting *Walz v. Tax Comm’n*, 397 U.S. 664, 674 (1970)). The Supreme Court’s decision in *Agostini v. Felton*, 521 U.S. 203 (1997), updated the application of the three-part test announced in *Lemon*. Under *Agostini*, the third prong’s prohibition on excessive entanglement is considered, but only as it relates to the second prong’s neutral effect requirement. *Id.* at 232–33. See William P. Marshall, *Constitutional Coherence and the Legal Structures of American Churches*, in RELIGIOUS ORGANIZATIONS IN THE UNITED STATES, *supra* note 121, at 759, 762 & n.17; see also Halcom, *supra* note 271, at 752–53 & n.170.

³³⁷ 493 U.S. at 389–90, 392; see *supra* notes 295–96 and accompanying text.

³³⁸ Halcom, *supra* note 271, at 752. However, with respect to the second *Lemon* prong, the breadth of the property tax exemption in *Walz*—“real estate owned by a wide array of nonprofit organizations”—was crucial to the Court’s ultimately sustaining the exemption. *Tex. Monthly, Inc. v. Bullock*, 489 U.S. 1, 11 (1989) (referring to *Walz*); see also Edward A. Zelinsky, *Are Tax “Benefits” for Religious Institutions Constitutionally Dependent on Benefits for Secular Entities?*, 42 B.C.L. REV. 805, 823 (2001) (remarking on the similarities between Justice Brennan’s majority opinion in *Texas Monthly* and his concurrence in *Walz*).

³³⁹ *Lemon*, 403 U.S. at 621–22; see also Edward McGlynn Gaffney, Jr., *Exemption of Religious Communities from State and Local Taxation*, in RELIGIOUS ORGANIZATIONS IN THE UNITED STATES, *supra* note 121, at 502–03; Thomas, *supra* note 228, at 628.

financial relationship between government and the religious organization, annual financial audits of the organization, and government scrutiny of the organization's religious versus secular expenditures.³⁴⁰ However, in *Lemon*, the Court conceded that "[s]ome relationship [or entanglement] between government and religious organizations is inevitable."³⁴¹ Accordingly, in subsequent decisions with respect to excessive entanglement, the Court has sanctioned generally applicable administrative and record-keeping requirements,³⁴² "routine regulatory interaction [such as application of neutral tax laws] which involves no inquiries into religious doctrine,"³⁴³ and fire inspections and building and zoning regulations.³⁴⁴ In *Walz v. Tax Commission*, the Supreme Court upheld a state property tax exemption for churches and other secular charitable organizations, acknowledging that "[g]ranting tax exemptions to churches necessarily operates to afford an indirect economic benefit and also gives rise to some, but yet a lesser, involvement than taxing them."³⁴⁵ Therefore, in comparing taxation of churches with granting them tax exemption, the Court observed that the latter results in less entanglement than the former.³⁴⁶

However, a religious-organization-based exemption does not always yield reduced entanglement. In *Texas Monthly, Inc. v. Bullock*, the Court determined that a state tax exemption granted only to religious publications violated the Establishment Clause.³⁴⁷ In addition to constituting a "statutory preference for the dissemination of religious ideas,"³⁴⁸ the narrow exemption also raised excessive entanglement issues. As in his

³⁴⁰ *Tilton v. Richardson*, 403 U.S. 672, 688 (1971). *Tilton* involved governmental grants, pursuant to Title I of the Higher Education Facilities Act of 1963, to several church-related colleges for purposes of constructing buildings to be used for secular purposes. *Id.* at 674–75. The *Tilton* Court distinguished the case from *Lemon* on the basis that colleges and universities, unlike elementary and secondary schools, are subject to less "sectarian influence." *Id.* at 685–86. However, the Court did invalidate a provision of the Act that limited the religious prohibition on buildings funded under the Act to twenty years, concluding that the possible religious use after that time period advanced religion in violation of the Establishment Clause. *Id.* at 683; see also Thomas, *supra* note 228, at 628.

³⁴¹ *Tilton*, 403 U.S. at 614; see also Halcom, *supra* note 271, at 753.

³⁴² *Hernandez v. Comm'r*, 490 U.S. 680, 696–97 (1989); see also Jimmy Swaggart Ministries v. Bd. of Equalization, 493 U.S. 378, 394 (1990).

³⁴³ *Hernandez*, 490 U.S. at 696–97.

³⁴⁴ *Lemon*, 403 U.S. at 614.

³⁴⁵ 397 U.S. 664, 674–75 (1970).

³⁴⁶ *Id.* at 676 ("The exemption creates only a minimal and remote involvement between church and state and far less than taxation of churches."); see also Halcom, *supra* note 271, at 753.

³⁴⁷ 489 U.S. 1, 25 (1989). The Texas statute exempted from sales tax all "[p]eriodicals that are published or distributed by a religious faith and that consist wholly of writings promulgating the teaching of the faith and books that consist wholly of writing sacred to a religious faith." *Id.* at 5 (quoting TEX. TAX CODE ANN. § 151.312 (1982)); see also *Budlong v. Graham*, 414 F. Supp. 2d 1222 (N.D. Ga. 2006) (declaring unconstitutional a sales tax exemption available only to religious organizations).

³⁴⁸ *Texas Monthly*, 489 U.S. at 28 (Blackmun, J., concurring).

Walz concurrence, Justice Brennan's plurality opinion in *Texas Monthly* concentrated on the breadth of the tax exemption.³⁴⁹ The Court ultimately concluded that the narrow exemption created greater state entanglement because it required public officials to determine the religious message or nature of the publications sold.³⁵⁰

By contrast, in *Jimmy Swaggart Ministries*, the Supreme Court concluded that the imposition of sales and use tax did not constitute unconstitutional entanglement between the state of California and the Ministries, a religious organization.³⁵¹ The organization argued that the imposition of the tax on its sale of religious materials resulted in on-site inspections and prolonged on-site audits, examinations of its financial records, threats of criminal prosecution, and numerous administrative and judicial proceedings.³⁵² Disputing the Ministries' factual assertions as to the state's entanglement, the Court concluded that "even assuming that the tax imposes substantial administrative burdens on appellant, such administrative and recordkeeping burdens do not rise to a constitutionally significant level."³⁵³ Because of the tax's secular purpose, general applicability, and failure to advance or inhibit religion, the Court concluded that the Establishment Clause's "core values are not even remotely called into question."³⁵⁴ Finally, the Court found most significant and persuasive the lack of required state inquiry into the religious nature of the items sold due to the tax's general applicability.³⁵⁵ "From the State's point of view," stated the Court, "the critical question is not whether the materials are religious, but whether there is a sale or a use, a question which involves only a secular determination."³⁵⁶

In specifically addressing Establishment Clause concerns raised by a nondiscrimination condition under the *Lemon* test, Professor Volokh observed that applying such a condition to all organizations receiving a subsidy, including religious ones, has an obvious secular purpose and does not primarily inhibit a particular religion.³⁵⁷ Volokh

³⁴⁹ *Id.* at 12 (majority opinion); see also Zelinsky, *supra* note 338.

³⁵⁰ *Texas Monthly*, 489 U.S. at 20.

³⁵¹ *Jimmy Swaggart Ministries v. Bd. of Equalization*, 493 U.S. 378, 396–97 (1990).

³⁵² *Id.* at 392.

³⁵³ *Id.* at 394–95 (citing *Hernandez v. Comm'r*, 490 U.S. 680, 696–97 (1989) ("[R]outine regulatory interaction [such as application of neutral tax laws] which involves no inquiries into religious doctrine, . . . no delegation of state power to a religious body . . . and no 'detailed monitoring and close administrative contact' between secular and religious bodies, . . . does not of itself violate the nonentanglement command.")).

³⁵⁴ *Id.* at 394.

³⁵⁵ *Id.* at 396.

³⁵⁶ *Id.*

³⁵⁷ Volokh, *supra* note 259, at 1945 (quoting *Bob Jones Univ. v. United States*, 461 U.S. 574, 604 n.30 (1983)). In response to the University's contention that the denial of its tax-exempt status violated the Establishment Clause because it preferred "religions whose tenets do not require racial discrimination over those which believe racial intermixing is forbidden," the Supreme Court stated that "a regulation does not violate the Establishment Clause merely because it 'happens to coincide or harmonize with the tenets of some or all religions.' The IRS policy at issue here is founded on a 'neutral, secular basis,' and does not violate the Establishment Clause." *Bob Jones Univ.*, 461 U.S. at 604 n.30 (citations omitted).

opined that entanglement issues will likely arise in the context of enforcing anti-discrimination laws or provisions, especially with respect to the hiring of clergy and other churches' leaders.³⁵⁸ While acknowledging the Supreme Court's decision in *NLRB v. Catholic Bishop of Chicago*, which addressed the potentially unconstitutional application of the National Labor Relations Act to teachers in religious schools,³⁵⁹ he recognized the trend of lower courts to permit the application of anti-discrimination law to such teachers.³⁶⁰ In such cases, he explained, the courts have determined that applying anti-discrimination law narrowly concentrates on particular hiring decisions, resulting in lesser amounts of entanglement than the broader sweep and involvement of labor law.³⁶¹ After vacillating about the potentially excessive entanglement resulting from the fact-finding required as to employment decisions, Volokh ultimately concluded:

[P]erhaps the antientanglement principle of the Establishment Clause counsels against closely scrutinizing groups' claims that they do not discriminate in clergy hiring and accepting groups' self-certification on the subject. But when they discriminate overtly, then the government can deny them a subsidy—alongside any other groups that discriminate—without excessively entangling itself with religious decisionmaking.³⁶²

Another legal commentator, Kenneth Halcom, uniquely approached the constitutional issues raised in this Article in the context of imposing a federal income tax on religious organizations.³⁶³ Although he addressed the Free Exercise Clause and other constitutional concerns, his analysis predominantly focused on the Establishment Clause. Taking into account the extensive connections between the government and religious organizations under current federal income tax law, Halcom concluded that the imposition of an income tax would not necessarily involve additional entanglements, but rather would significantly expand the ones that currently exist.³⁶⁴ Accordingly, he concluded that an income tax would foster excessive governmental entanglement with religion under a *Lemon* analysis, thereby violating the Establishment

³⁵⁸ Volokh, *supra* note 259, at 1946–47 (citing *EEOC v. Catholic Univ. of Am.*, 83 F.3d 343, 462 (D.C. Cir. 1996) (finding that churches have the “fundamental right . . . to ‘decide for themselves, free from state interference, matters of church government as well as those of faith and doctrine’” (citation omitted))).

³⁵⁹ 440 U.S. 490, 502 (1979).

³⁶⁰ Volokh, *supra* note 259, at 1947.

³⁶¹ *See id.* (quoting *Geary v. Visitation of the Blessed Virgin Mary Parish Sch.*, 7 F.3d 324, 328 (3d Cir. 1993) (stating that labor law would “inject the Board into ‘nearly everything’ that occurs in a religious school”)).

³⁶² *Id.* at 1949.

³⁶³ *See* Halcom, *supra* note 271.

³⁶⁴ *Id.* at 760.

Clause.³⁶⁵ The logical corollary to this conclusion, therefore, is that the Constitution requires religious organizations to be exempt from income tax.³⁶⁶

However, Halcom astutely noted that the Constitution does not necessarily require that religious organizations be granted exemption of the kind statutorily provided by § 501(c)(3).³⁶⁷ A religious organization, therefore, need not be eligible to receive deductible charitable contributions or to issue tax-exempt bonds.³⁶⁸ By drawing a distinction between constitutionally required and statutorily granted exemptions, Halcom contended that the IRS could revoke a religious organization's tax-exempt status under § 501(c)(3) for violating one of its statutory conditions without implicating any constitutional issues, provided the IRS "does not seek to recover income taxes" from that organization pursuant to § 61.³⁶⁹ Therefore, Congress may place limitations on § 501(c)(3) tax-exempt status without constitutional implications provided the religious organization is not ultimately required to pay income tax.³⁷⁰ Accordingly, under his analysis, Halcom would phrase the issue raised in this Article not as whether a religious organization that discriminates should continue to be tax-exempt, but whether donors to that organization should continue to deduct their contributions under § 170 and whether the organization should continue to be eligible for tax-exempt financing under § 145.³⁷¹

C. Analysis

In determining the constitutionality of imposing a nondiscrimination requirement on the tax exemption of religious organizations under § 501(c)(3), the analysis seems to focus primarily on the Establishment Clause. With respect to free speech or associational rights under the First Amendment, case law consistently supports the notion that tax exemption is a privilege, not a right, and that Congress can choose to not subsidize certain activities, such as lobbying or involvement in political campaigns.³⁷² However, to date, the Supreme Court has not addressed whether denying or revoking an organization's tax-exempt status based on its discriminatory membership policy or other exclusionary practice violates that organization's First Amendment rights to expressive association.³⁷³ Nevertheless,

³⁶⁵ *Id.* at 762.

³⁶⁶ *Id.* at 766.

³⁶⁷ *Id.* at 767.

³⁶⁸ *See id.* at 767–68.

³⁶⁹ *Id.* at 767. He also notes that "[f]or substantially the same reasons, Congress may at any time repeal section 501(c)(3) and the entire tax-exemption regime." *Id.* at 767 n.254. Furthermore, if an organization engages in excessive lobbying or political campaign activities, it will lose its "religious character and its corresponding First Amendment protection." *Id.* at 767.

³⁷⁰ *Id.* at 768.

³⁷¹ *Id.* at 773.

³⁷² *See supra* notes 229–58 and accompanying text.

³⁷³ *See* Brennen, *supra* note 225; Mirkay, *Charities & Discrimination*, *supra* note 5, at 72.

the Court has sustained limitations on other First Amendment rights of charitable organizations as a condition to tax exemption under § 501(c)(3),³⁷⁴ in part due to the ability of those organizations to qualify for tax exemption under § 501(c)(4) as social welfare organizations.³⁷⁵ This is the constitutional safe harbor to which Justice Blackmun alluded in his *Regan* concurrence.³⁷⁶

The Free Exercise Clause also should not be implicated because the proposed nondiscrimination requirement would be broadly applied to all nonprofits seeking or maintaining tax-exempt status under § 501(c)(3) and would be religiously neutral.³⁷⁷ Furthermore, the nondiscrimination requirement does not constitute a prior restraint on the free exercise of religious beliefs in that it does not attempt to prohibit or prevent the observance of religious beliefs, as in *Murdock* or *Follett*.³⁷⁸ Rather, it only limits the benefits conferred under § 501(c)(3) in addition to tax exemption—the charitable contributions deduction and the ability to issue tax-exempt bonds. Even if the nondiscrimination requirement was asserted to be a substantial burden on an organization's free exercise of its religious beliefs, as in *Branch Ministries*, the revocation or denial of exemption would likely be viewed as a non-constitutionally significant burden,³⁷⁹ especially with respect to churches where the impact would be "more symbolic than substantial."³⁸⁰ Nevertheless, the RFRA and its state progeny do raise some perplexing free exercise questions, the answers to which can only be hypothesized currently by a preeminent constitutional law scholar.³⁸¹ The uncertainty surrounding a RFRA-based free exercise claim ostensibly supports this Article's conclusion of exempting a "church"—as a narrowly defined term—from the proposed nondiscrimination requirement. It will specifically avoid any excessive entanglement with respect to the hiring of clergy and other employees that implement the church's purely religious functions.

³⁷⁴ For instance, the Court has upheld statutory limitations under § 501(c)(3) on religious and other charitable organizations' lobbying and political campaign activities. See *supra* notes 230–58 and accompanying text.

³⁷⁵ See *supra* note 56. One could argue, however, that discriminatory policies or practices conflict with the regulatory definition of social welfare:

An organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the community. An organization embraced within this section is one which is operated primarily for the purpose of bringing about civic betterments and social improvements.

Treas. Reg. § 1.501(c)(4)-1(a)(2)(I) (as amended in 1990).

³⁷⁶ See *supra* notes 242–43 and accompanying text.

³⁷⁷ See *supra* notes 279–311 and accompanying text.

³⁷⁸ See *supra* notes 286–87 and accompanying text.

³⁷⁹ See *supra* note 309 and accompanying text.

³⁸⁰ See *supra* note 310 and accompanying text.

³⁸¹ See Volokh, *supra* note 259, at 1963–64; see also Eugene Volokh, *Intermediate Questions of Religious Exemptions—A Research Agenda with Test Suites*, 21 CARDOZO L. REV. 595, 610–13, 630–34 (1999).

With respect to a nondiscrimination restriction on § 501(c)(3) exemption, the primary issue ostensibly involves the Establishment Clause—namely, whether such a restriction would constitute “excessive government entanglement with religion.”³⁸² Under current federal income tax law, “extensive connections” exist between religious organizations and the government via the IRS.³⁸³ These connections include (i) an application for recognition of exemption (except churches),³⁸⁴ (ii) record retention requirements,³⁸⁵ (iii) an annual information return (except churches),³⁸⁶ (iv) withholding taxes on employees,³⁸⁷ (v) payment of unrelated business income tax,³⁸⁸ and (vi) statutory limitations on exemption—prohibition on private inurement and political campaign activities and limitations on lobbying.³⁸⁹ Of course, the connections with churches are far less extensive because churches are generally only subject to withholding tax and unrelated business income tax requirements.³⁹⁰

Therefore, would an additional restriction limiting a religious organization’s policies and practices increase these connections to a level that constitutes “excessive entanglement,” thus triggering Establishment Clause problems? According to Halcom, Congress may place limitations on § 501(c)(3) income tax exemption without constitutional implications, provided the religious organization retains its constitutionally required exemption.³⁹¹ In other words, the organization is not ultimately required to pay income tax under § 61 even if its exemption is denied or revoked. Professor Volokh was less confident about a non-entanglement result in such contexts, ultimately concluding that caution should be exercised particularly with respect to hiring clergy and that organizations’ claims that they do not discriminate in such contexts should be accepted generally at face value.³⁹² Once again, Volokh’s conclusion ostensibly supports this Article’s judgment to exercise caution and exempt a “church”—as a more narrowly defined term—from the proposed nondiscrimination requirement.

³⁸² *Lemon v. Kurtzman*, 403 U.S. 602, 612–13 (1971) (quoting *Walz v. Tax Comm’n*, 397 U.S. 664, 674 (1970)).

³⁸³ Halcom, *supra* note 271, at 756.

³⁸⁴ I.R.C. § 508 (2000).

³⁸⁵ I.R.S. Announcement 94-111, 1994-37 I.R.B. 36; *see also* I.R.S., TAX GUIDE FOR CHURCHES AND RELIGIOUS ORGANIZATIONS 20 (2008), <http://www.irs.gov/pub/irs-pdf/p1828.pdf> [hereinafter TAX GUIDE].

³⁸⁶ I.R.C. § 6033.

³⁸⁷ TAX GUIDE, *supra* note 385, at 18–19.

³⁸⁸ *See* I.R.C. §§ 511–514. Although originally exempt, churches have been subject to the unrelated business income tax since the Tax Reform Act of 1969. *See supra* note 135 and accompanying text.

³⁸⁹ *See supra* notes 76, 82–85 and accompanying text.

³⁹⁰ Halcom, *supra* note 271, at 758.

³⁹¹ *Id.* at 766.

³⁹² Volokh, *supra* note 259, at 1946.

CONCLUSION

With respect to the separation of church and state, contemporary legal scholars astutely observe the implausibility of separating church and state in modern times: “Church and state are not separate in the United States, and could not possibly be separate. The question is not *whether* the state should be permitted to affect religion, or religion permitted to affect the state; the question is *how* they should be permitted to affect each other.”³⁹³ This Article addressed the latter question of how religious organizations, including churches, and the government should affect each other in the context of tax exemption and public benefit. Specifically, it proposed a broad nondiscrimination condition on tax-exempt status under § 501(c)(3). A religious organization should not continue to enjoy the benefits of that tax-exempt status if it engages in discrimination, because it is intrinsically incompatible with its purpose and mission as a charitable organization.

A nondiscrimination requirement in § 501(c)(3) presents a more comprehensive solution to the problem of discriminatory policies and practices in religious organizations than any expanded application of the public-policy doctrine or current civil rights laws. It would send a strong message that discrimination is fundamentally inconsistent with tax-exempt status under § 501(c)(3), thereby bolstering “the commonly held view that discrimination is generally wrong and thus generally should not be subsidized by the government. . . .”³⁹⁴ The intent of a statutorily imposed nondiscrimination condition is not to control or regulate religious beliefs, but to eliminate the use of tax-deductible dollars, and other benefits received by religious organizations pursuant to § 501(c)(3), to support or maintain discrimination against members of society.

Because this Article focused on religious organizations and churches, its proposal creates many challenges, primarily constitutional in nature. Nevertheless, by permitting discriminatory organizations to qualify as tax-exempt social-welfare organizations under § 501(c)(4), a nondiscrimination condition on § 501(c)(3) tax-exempt status should alleviate any First Amendment free speech or association concerns. In an attempt to avoid any potential Free Exercise or Establishment Clause concerns, churches, as a narrowly defined subset of religious organizations, should be excepted from the nondiscrimination requirement. The definition of a church, however, should be confined to the IRS fifteen-point test³⁹⁵ with a particular emphasis on the criterion of an established and dynamic congregation. In addition, Congress should likewise narrow a religious organization’s eligibility for “integrated auxiliary” status, thereby

³⁹³ Richard W. Garnett, *Religion and Group Rights: Are Churches (Just) Like the Boy Scouts?*, 22 ST. JOHN’S J. LEGAL COMMENT. 515, 519 (2007) (quoting CHRISTOPHER L. EISGRUBER & LAWRENCE G. SAGER, *RELIGIOUS FREEDOM AND THE CONSTITUTION* 6–7 (2006)).

³⁹⁴ Volokh, *supra* note 259, at 1934.

³⁹⁵ See *supra* note 104 and accompanying text.

limiting the organizations functionally treated as churches under the Code. By statutorily limiting an integrated auxiliary's non-church funding to twenty percent or less, Congress would be providing "a fair, objective test . . . without questioning the religious nature of any particular organization."³⁹⁶ Furthermore, a lower non-church-funding threshold would accomplish Congress's objective of subjecting more tax-exempt organizations to public disclosure and inspection.

Although this Article proposes some solutions, its primary intent is to further the dialogue on how best to resolve the inherent tension that exists when government provides tax benefits to discriminatory organizations. As one legal scholar explained, "We do not in the abstract resolve the tension between respecting religious groups and ensuring each individual protection against discrimination; nor do we resolve it quickly. Instead, we struggle over time, in courts, legislatures, private settings, and complex negotiations."³⁹⁷ Perhaps this dialogue and struggle will compel religious organizations to accentuate differences less and utilize the benefits of their tax-exempt status more to further social justice and combat social ills such as poverty and hunger, which know no boundaries of age, gender, religion, race, ethnicity, or sexual orientation.

³⁹⁶ STAFF OF JOINT COMM. ON TAXATION, 98TH CONG., GENERAL EXPLANATION OF THE REVENUE PROVISIONS OF THE DEFICIT REDUCTION ACT 1214 (Comm. Print 1984).

³⁹⁷ Minow, *supra* note 184, at 848.